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Texas Community Reinvestment 2007 Update

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Community Reinvestment in Texas: Update 2007

Executive Summary

In 1997, the 75th Legislature enacted House Bill (HB) 1414. This legislation formed the Community Reinvestment Work Group to develop statewide community reinvestment strategies using investment pools and other investment vehicles that leverage private capital from banks, insurance companies and other entities for community investment in Texas. As specified in the legislation, the Community Development Work Group is composed of representatives of the Texas Department of Banking, Texas Comptroller of Public Accounts, Texas Department of Housing and Community Affairs, Economic Development and Tourism Division of the Governor's Office and the Texas Department of Insurance. Title V, Chapter 395 of the Texas Finance Code requires the work group to consult with appropriate federal regulatory agency representatives of the Office of the Comptroller of the Currency, the Federal Reserve Board of Governors (FRB), the Office of Thrift Supervision (OTS) and the Federal Deposit Insurance Corporation (FDIC). The work group monitors and evaluates community reinvestment strategies; ensures that the strategies encourage financial institutions to lend money to Texas' low-income and moderate-income families and individuals; and coordinates efforts to attract private capital through investments that meet the requirements of the Community Reinvestment Act of 1977 (12 U.S.C. Section 2901 et seq.).

Each biennium, the Community Reinvestment Work Group summarizes the effectiveness of the group's strategies developed under Chapter 395 of the Texas Finance Code.

The following agencies contributed to the 2007 update on Community Reinvestment in Texas:

- Texas Department of Banking,
- Texas Comptroller of Public Accounts,
- Texas Department of Housing and Community Affairs,
- Economic Development and Tourism Division of the Governor's Office,
- Texas Department of Insurance,
- Texas Association of Community Development Corporations,
- Office of Rural and Community Affairs, and
- Texas Low-Income Housing Information Service.

The work group met in 2006 to discuss the effectiveness of current agency community reinvestment strategies, public and private sector community reinvestment initiatives and developed new strategies for 2007-2008. The Comptroller's work group representative interviewed representatives of banks, research organizations, community reinvestment advocacy groups and federal regulatory agencies, including the Federal Deposit Insurance Corporation (FDIC) and the Federal Reserve Bank (FRB) of Dallas.

This update gives an overview of the Community Reinvestment Act (CRA), describes changes to CRA regulations that became effective September 1, 2005 and highlights recent data and available studies on small business, small farm and community development lending in Texas. The update also outlines community reinvestment strategies of the state's banking, economic development, housing, and insurance agencies and gives examples of community reinvestment initiatives in Texas.

Recent Legislation

In 2005, the 79th Legislature enacted several consumer protection bills to assist Texas homebuyers and support community investment:

- House Bill 1823 established new protections for contract-for-deed and rent-to-own buyers in Texas. This legislation gives consumers the right to convert a contract-for-deed into a traditional mortgage, stops excessive late fees and prohibits sudden termination of the "option to buy" in rent-to-own programs.
- House Bill 525 passed as an effort to prevent the displacement of working and retired, lower income individuals and families from East Austin. The bill creates opportunities for low and moderate-income families to own homes, authorizes the

city to create a development district known as the Homestead Preservation District through land trusts, land banks and tax increment financing dedicated to city-certified community housing development organizations.

- House Bill 1099 transferred farm worker housing inspection authority to the Texas Department of Housing and Community Affairs (TDHCA) from the Texas Department of Health (TDH).
- House Bill 1582 directed TDHCA and the Texas Savings and Loan Department to create a commission of experts to report by September 1, 2006 on mortgage foreclosure rates in Bexar, Cameron, Dallas, El Paso, Harris and Travis counties. A summary of the commission's results is included in Appendix E.
- Senate Bill 1186 closed loopholes that denied active U.S. service members and domestic violence victims the right to terminate their apartment leases.
- Senate Bill 356 created a land bank program for Houston, Texas, which allows Houston to sell tax foreclosed property to organizations for affordable housing development.
- House Bill 467 expanded the Economically Distressed Areas Program (EDAP) that supplies water and sewer services to low income communities of the state. The bill makes no-interest loans and grants available from the state for impoverished areas without water and sewer services. However, there is no available funding for the program.
- House Bill 2491 amendments made the elderly homestead exemption automatic at age 65.

From its research, the Community Reinvestment Work Group concluded that:

- Texas' 1.9 million small businesses provide the largest source of jobs in the state.[1]
- Texas law does not require separate disclosure of insurers' investments in low- and moderate-income communities. Life and health insurers, however, voluntarily reported in 2006 to the Texas Department of Insurance investments of $760 million in the state's economically disadvantaged areas for 2005.[2]
- The 2006 survey of Community Development Corporations (CDCs) and Community Development Financial Institutions (CDFIs) by the Texas Association of Community Development Corporations (TACDC) identified more than $216 million in loans by CDFIs to community businesses and residents in Texas in 2005. Of 259 survey respondents, 210 reported producing affordable housing or planning to pursue housing production in 2006-07. Responding CDCs indicated they built more than 53,000 affordable housing units in 2005 with plans to construct another 5,100 units between 2006 and 2007.[3]
- The Texas Department of Banking reported bank- and thrift-insured deposits in Texas of $402.5 billion as of June 2006. More than half of these deposits were controlled by 49 out-of-state institutions, and 654 Texas-chartered institutions control the rest.[4]
- The Texas Department of Housing and Community Affairs (TDHCA) administers more than $400 million annually as the state's lead agency for affordable housing and community assistance programs. Ninety-two percent of the households served by TDHCA housing programs in fiscal 2005 were low-income, earning no more than 80 percent of the area median family income (AMFI).[5]
- The Linked Deposit Program continues to provide loans to minority and women-owned businesses, child-care centers, non-profit organizations and small businesses located in state-designated enterprise zones. The program is a partnership of the Comptroller's office, approved depository lenders and the Governor's Economic Development and Tourism office.

The Community Reinvestment Act (CRA): 1977-2006

Passed by Congress in 1977, the Housing and Community Development Act (CRA) encourages commercial banks and savings and loans to help meet the credit needs of all segments of the communities where they operate.[6] The CRA was one of the first legislative acts passed by the U.S. Congress to address redlining by banks and savings and loan institutions. CRA applies to all federally insured depository institutions, national banks, thrifts and state-chartered commercial and savings banks.

Community Development and CRA Goals

The CRA's main goal is to improve access to credit for businesses and individuals in low- and moderate-income communities. Initially, Congress aimed to resolve geographic discrimination by financial institutions that didn't meet the credit needs of communities where they were chartered. Since CRA's passage in 1977, the Act has helped affordable housing and community development advocates evaluate the lending performance of CRA-regulated financial institutions while improving home ownership opportunities to underserved populations.

Financial institutions comply with the CRA's requirements for meeting the credit needs of communities by making loans to support:

- building and rehabilitation of affordable housing and permanent financing for multifamily rental property for low- and moderate-income persons;
- community development activities of local, state and tribal governments including financing for geographic areas recovering from natural disasters and middle-income census tracts in distressed or under-served rural counties;
- community development corporations (CDCs), community financial institutions (CDFIs) and minority- and women-owned financial institutions;
- community services targeted to low- and moderate-income individuals including credit and homebuyer counseling, school savings programs, technical assistance for economic revitalization programs and other activities;
- construction of community facilities in low- and moderate income areas; and
- financing for environmental clean up activities and redevelopment of industrial sites in low- and moderate-income communities.

The Financial Services Industry and the CRA

The U.S. financial industry has evolved since the 1977 passage of the CRA. Some changes resulted in response to market forces, consolidation of large and small banks, deregulation of the banking industry and the effects of technological advances. In the past 30 years, banks and other financial institutions benefited from financial industry competition, check cashing and credit card services, the marketing of insurance products and sales of securities across state lines. Companies in the financial and insurance services sectors have expanded into mortgage banking, providing loans without traditional banking regulatory oversight.

Changes in the U.S. economic, financial and environments prompted amendments of CRA regulations three times in the past 30 years—1989, 1995 and 2005. Originally, the CRA was enacted to address the depressed condition of lower-income and minority neighborhoods in American cities in the 1970s. The CRA was only one of a number of bills passed by Congress at the time to promote access to credit, reduce lending discrimination and make loans and lending more transparent. Examples of related legislation included the Equal Credit Opportunity Act and the Home Mortgage Disclosure Act.

Congress passed the Financial Institution Reform and Recovery Act of 1989 (FIRREA) due to public concern over continued access to credit issues. This law created four CRA ratings to reflect a supervised bank's compliance with the CRA: 1 for outstanding, 2 for satisfactory, 3 for needs to improve and 4 for substantial noncompliance. The act also required public disclosure of CRA examination ratings and written evaluations by regulatory agencies. By the mid-1990s, the public's worry about the growth of bank acquisitions and mergers prompted Congress to enact the Riegle-Neal Interstate

Banking and Branching Efficiency Act of 1994. This legislation led banks to direct more resources to their CRA programs to develop plans for managing their CRA activities to comply with new regulations.

The 1980s and 1990s brought banking deregulation and technological advances in the form of improved data retrieval, processing and storage and the use of credit-scoring. By 1994, the Community Development Financial Institutions Act (CDFI) was passed, which opened up new community development financial opportunities. In 1995, other CRA regulations changed to create a lending test for large banking institutions to promote innovation to meeting credit needs for community development. Regulatory agencies planned to review the CRA again in 2002 for effectiveness of the changes made in 1995. By 2005, banking and community organization advocates agreed that the CRA regulation structure was sound. The regulatory agencies' research led to several new definitions for "small" banks including an "intermediate small" bank and the expansion of the meaning of "community development."[7]

History of CRA Rules

Amendments to CRA regulations have enhanced the public's accessibility to CRA examination schedules, results and related data. The changes have also expanded the options for investment by financial institutions that count as credit toward their CRA compliance rating.

Congress passed the Financial Institution Reform, Recovery, and Enforcement Act (FIRREA) in 1989. This created four composite CRA ratings to reflect a supervised bank's compliance with the CRA: 1 for outstanding, 2 for satisfactory, 3 for needs to improve and 4 for substantial noncompliance. The act also required public disclosure of CRA examination ratings and written evaluations by regulatory agencies.

In 1991, Congress passed a second amendment requiring public discussion of a regulator's evaluation of financial institutions' CRA performance to allow community groups to discuss results with regulators. A third amendment followed in 1992 that allows CRA regulators to provide their supervised banks credit under the CRA for investing in minority- and women-owned financial institutions and low-income credit unions.

An amendment enacted in 1994 requires institutions with interstate branches to receive a separate examination and rating for each state in which they conduct business. This amendment mandates separate evaluations for banks with branches in two or more states in the same metropolitan area. In 1995, revised regulations implemented three tests—a lending, investment and service test, with the lending test carrying most of the weight in calculating total CRA credit.[8]

In 2002, Section E of the CRA was enacted to prohibit any bank or branch of a bank controlled by an out-of-state bank holding company from establishing or requiring a branch or branches out of its home state under the Riegle-Neal Act, primarily for the purpose of deposit production.

Effective January 1, 2003, a Federal Reserve Board amendment required lenders to ask applicants their national origin or race and sex in loan applications taken by telephone. The telephone application rule now applies to mail and Internet applications.

As of January 1, 2004, HMDA and CRA reporters were required to use the June 6, 2003 geographic statistical area designations provided by the U.S. Office of Management and Budget (OMB) for data collection and reporting in March 2005. OMB's revised metropolitan statistical area boundaries led to changes in definitions updated in February 2004 and effective December 2003. The terms MSAs (used in lieu of metropolitan area) and MetroDivs (Metropolitan Divisions) became required for HMDA and CRA reporting. The $25 million volume test was added to the existing percentage-based coverage test for non-depository lenders. The asset threshold for depository lenders was raised to $33 million for 2004 data collection and remained unchanged at $10 million or less for non-depository institutions.

Starting March 21, 2005, a change from 2004 required lenders to collect and report additional data on home loans and financing for manufactured homes, including loan pricing information, lien status, e.g., secured by a first or subordinate lien, or unsecured lien.[9]

Increasing numbers of lenders sought liquidity in the mid- and late-1990s by selling primary mortgages to obtain funds to originate new loans. The secondary mortgage market grew, and the total number of home mortgage loans by financial institutions increased. Internet technology advances encouraged consumers to seek loans and pay bills online. Banks continued to consolidate and banks implemented credit scoring software programs to determine a prospective borrower's ability to repay debts and loans.

In August 2004, the OTS expanded the category of "small savings associations" to include those with less than $1 billion in assets, regardless of affiliate holding company affiliation.[10]

Competition continues to heat up among financial service institutions. In 2006, credit unions exempt from federal taxes and CRA requirements, enlarged their portfolios at rates similar to FDIC-insured institutions while posting greater growth rates in credit card balances and real estate loans. During that year, credit union deposit growth lagged behind that of banks, and bank interest income jumped 23 percent, while credit union interest income grew only 16 percent. This resulted in a tighter net interest margin for credit unions.

While the banking industry continues to consolidate, the U.S. witnessed the largest year of growth in 2005 of new community banks opened for business since 1999. The U.S. has about 9,000 community banks, including commercial banks, thrifts and savings institutions. Community banks make up 95 percent of all banks and continue proliferating, according to the Independent Community Bankers of America. While the total number of banks is decreasing across the U.S., community-based banks continued growing in terms of asset quality, capital and earnings in 2005 and 2006, according to Governor Susan Schmidt Bies at the Federal Reserve Board.[11]

Evaluations of Financial Institutions

Federally-insured depository institutions, national banks, savings associations, state-chartered commercial and savings banks must comply with CRA regulations. Four separate federal agencies—the FDIC, the FRB, the OCC and the OTS—evaluate the CRA record of institutions they regulate before approving applications for charters or for approval of mergers, acquisitions, and branch openings. (See Appendix A for details on the evaluation process and changes to the definition of small banks.)

The FDIC conducts CRA examinations of state-chartered institutions that are not a member of the Federal Reserve System. The Governors of the Federal Reserve System regulates state-chartered banks that are members of the Federal Reserve System, bank holding companies and branches of foreign banks.[12] The FDIC, the OCC and the OTS examine depository institutions not supervised by the FRB. The FRB considers the CRA record of its member banks before approving applications to open new deposit-taking facilities.

CRA regulation 12 CFR 25 requires the OCC to conduct CRA exams of national banks every three years. The regulation also requires the OCC to assess a national bank's record of helping meet credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operations before approving any applications requesting to merge bank operations.[13]

Under the CRA regulation 12 CFR Part 563e, the OTS is required to assess a savings association's record of helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operations. OTS must also consider that record in its evaluation of a savings association's application for new branches or relocation of an existing branch, mergers and consolidations and other corporate activities.[14]

Changes in CRA Rules in 2005 and 2006

Revised Community Reinvestment Act rules became effective September 1, 2005. The Office of the Comptroller of the Currency noted "the CRA has been beneficial for banks and communities, but complying with the CRA was a burden for smaller banks." Regulators' changes to the CRA in 2005 helped lessen the data collection and reporting requirements for small community banks and encourage community development activities in designated disaster areas and distressed and underserved rural areas. The 2005 changes do not affect thrifts regulated by the Office of Thrift Supervision.

Small Banks and Intermediate Small Banks

"Small bank" describes a bank that had assets of less than $1.033 billion as of December 31 of either of the prior two calendar years. This change became effective January 1, 2007. Effective September 1, 2005, new CRA rules helped relieve about 1,800 intermediate small banks with $250 million to $1 billion in assets from previous CRA data collection requirements and from testing of bank investments and service to their respective communities.

A second small bank definition was created by the FDIC, the FRB and the OCC, called the "Intermediate small bank (ISB)." This applies to small banks with assets of at least $258 million as of December 31 of both of the prior two calendar years and less than $1.033 billion as of December 31 of either of the two prior calendar years. Regulators will continue evaluating small banks using a streamlined small bank lending test.

In 2005, new CRA rules replaced the investment, lending and service tests with two separately rated tests for ISBs. These two tests are the existing lending test for small banks and a new community development test for ISBs. The lending test evaluates five performance criteria including the loan-to-deposit ratio, lending in and out of the assessment area, responses to complaints, the geographic distribution and the borrower distribution of loans.[15] The ISB test was designed to allow ISBs more say in the way they structure community development activities to meet community development needs in their assessment areas. An ISB may choose to be evaluated as a large bank under the three-part lending, investment and service test if the bank collects and submits required loan data outlined in regulation 12 CFR 25.21(a)(3). ISBs did not have to submit any collected CRA data in 2005 and 2006.[16] Regulators will judge an ISB on its business strategy, bank capacity and the community development needs of the ISB's local service area. The community development test does not consider retail banking services and does not review a bank's record of opening and closing branches.[17]

Large Banks

"Large" banks, defined by the regulatory agencies, have total assets of at least $1.033 billion on December 31 of both of the previous two calendar years. Large banks are required to collect and submit CRA loan data, but are not examined with a large bank test until their bank has collected one full year of data. Any size bank may choose to be examined with the large bank test if it has collected and submitted required CRA loan data. Regulators will continue to evaluate large banks using the lending, investment and service test once every two years to grade the lending institution's lending, investments and services in low- and moderate-income neighborhoods. Large bank examinations are based on lending, investment and service performance and must disclose data on their mortgage lending in non-metropolitan areas, community development activities and to small businesses. An unsatisfactory or weak CRA record can result in the denial of a financial institution's requests to expand operations.

Small Savings Associations

For "small savings associations," the OTS proposed in 2006 to align its CRA rules with the FDIC, the FRB and the OCC. The proposed regulation would change the definition of "small savings associations" with $251 million to $1 billion in assets to "intermediate small savings associations" and establish a new community development test for them; eliminate the option for alternative weighting under the large retail savings association test; index asset thresholds based on changes to the Consumer Price Index (CPI); and clarify the impact of discrimination on an association's CRA rating.[18] The change would end the option to choose alternative weights for lending, investment and service under the large, retail savings association test, create a new community development test for thrifts holding assets between $250 million and $1 billion; and annually index the asset threshold for small and intermediate small associations in line with Consumer Price Index (CPI) changes.

CRA Regulatory Examinations

Examiners customize federal regulatory tests to examine limited purpose and wholesale banks that specialize in large commercial deposits and provide credit cards but do not make home loans or accept small deposits. Customized tests focus on the number of community development loans and investments, including low-income housing tax credits or investments in small businesses that a bank has made in its service area.

Each quarter, the four federal regulatory agencies publish lists of CRA examination schedules for CRA-regulated banks and savings institutions. Regulators maintain the lists on their agency Web sites and provide them to the public.

The OCC examines banks on a cycle determined by the bank's asset size and performance on previous examinations. Banks with more than $250 million in assets fall in the risk-based cycle, which begins 36 months after the bank's previous OCC examination. Under the Gramm-Leach-Bliley Act, the OCC follows an extended exam cycle for small banks with aggregate assets of $250 million or less and an overall outstanding CRA rating. OCC exams of small banks with an overall CRA rating of satisfactory cannot begin sooner than 48 months after its most recent exam and no earlier than 60 months after its last CRA exam if it was ranked "Outstanding" on its last exam. The OCC may remove banks from the extended exam cycle when a bank has applied for a depository facility or for reasonable cause.

Under the new 2005 CRA rules, a bank must receive a "satisfactory" on the community development and lending tests before it can open new deposit-taking branches. The new community development test analyzes four areas of bank activity: affordable housing, community services, economic development, revitalization and stabilization activities.

The affordable housing and community services evaluation applies to low- or moderate-income individuals. The economic development evaluation applies to small businesses and farms, and the revitalization or stabilization analysis evaluates bank services provided to low-or moderate-income census tracts or underserved rural areas.[19]

The OCC widened the definition of community development to include activities that stabilize and strengthen designated disaster areas and "underserved and distressed" rural areas.[20]

The Office of Thrift Supervision (OTS), monitors data collection and reporting for OTS-regulated small banks. All savings associations, except small institutions, are subject to data collection and reporting requirements.

- A small OTS institution is a thrift with under $1 billion in assets as of December 31 of either of the prior two calendar years.[21]
- The OTS uses a streamlined examination under CRA regulations for "small institutions," which focuses on the institution's lending record.[22]
- A rule created by the FDIC, FRB and OCC in August 2005: 1) created a new community development test for intermediate small banks with assets between $250 million and $1 billion; 2) provided criteria for evidence of discrimination or practices in violation of laws, rules or regulations that may negatively affect the CRA rating of an institution; 3) adjusted regulated institutions' asset thresholds annually for inflation by the Consumer Price Index (CPI); and 4) tightened evaluation options for large banks in the areas of lending, investment and services by maintaining weight allocations of 50 percent on lending, 25 percent on investments and 25 percent on services.

To be consistent, OTS revised its rule in March 2007 to align its CRA regulation with those of the other federal banking regulatory agencies. The rule takes effect July 1, 2007 with rule changes applying to exams beginning in the third quarter of 2007.[23]

Lending institutions of any size can choose to develop a strategic plan instead of being examined by regulators. The strategic plan option allows the financial institution to structure its CRA evaluation criteria and objectives to the unique needs of the community it serves based on its own lending capacities, banking strategies and expertise.

The Gramm-Leach-Bliley (GLB) Act and the CRA

Following the Great Depression, Congress originally passed the Glass-Steagall Act to eliminate high-risk financial behavior including uninsured deposits in questionable securities. The Gramm-Leach-Bliley (GLB) Act, known as the Financial Services Modernization Act of 1999, repealed restrictions found in sections 20 and 32 of the Glass-Steagall Act of 1933 concerning the affiliation of banks and securities firms. The GLB Act ended legal barriers among the banking, insurance and securities industries, which allowed them to combine services and provide financial products. The GLB Act also created a system for federal and state financial regulatory compliance, requiring the Federal Reserve Board to supervise financial holding companies.

Under the GLB Act, state insurance departments were designated as the functional regulators of the insurance business activities of banks and all financial firms involved in the business of insurance. The GLB Act created new forms of financial institutions called "Financial Holding Companies" (FHCs) as part of section 4 of the Bank Holding Company Act.[24] The GLB Act requires that financial holding companies, insured depository institutions affiliated with a financial holding company or stand-alone insured depository institutions may only be approved for expanded activities or acquisitions if its latest CRA examination rating is satisfactory or better.

Regulatory examiners use the Federal Financial Institutions Examination Council's (FFIEC) revised interagency examination procedures to assess financial institutions' compliance with the provisions in the CRA "Sunshine Requirements" of the Gramm-Leach-Bliley Act (GLBA). Generally, sunshine provisions require all parties to an agreement to file a report with the appropriate regulatory agency each year and require examiners to investigate and describe the institution's covered agreement disclosure practices. Effective April 1, 2001, the CRA Sunshine Requirements make agreements between or among agencies, nongovernment entities or persons, FDIC-insured banks or savings institutions that accept deposits and their affiliates to make the agreements available to the public and to file annual reports with the appropriate federal banking agency. The CRA Sunshine Requirements apply to funds of an insured depository institution or any affiliate with an aggregate value of more than $10,000 in a calendar year and financial institutions having loans with aggregate principal value of more than $50,000 in a calendar year.[25] When management determines that a financial institution is a party to one or more covered agreements, the regulation requires examiners to investigate and describe the institution's covered agreement disclosure practices.

Home Mortgage Disclosure Act (HMDA) Data Disclosure

Enacted by Congress in 1975, the Home Mortgage Disclosure Act (HMDA) requires most mortgage lenders in metropolitan areas to collect data on housing-related lending activity. Lenders must report this data to the government annually and ensure that the data is publicly available. HMDA data apply to transactions for home improvement loans, purchases and refinancings. Under the CRA, agencies that evaluate insured depository institutions use HMDA data when evaluating banks, savings and loan associations, credit unions and mortgage and consumer finance companies' records of helping meet their communities' mortgage credit needs.

Originally, HMDA was used to help determine whether financial institutions serve the housing needs of their communities and to enforce fair lending practices. Combined with the Federal Reserve Board's Regulation C, HMDA requires the majority of depository institutions and certain for-profit, non-depository institutions to collect, report and disclose data concerning originations and purchases of home purchase and improvement loans, refinancing of homes and related loan applications.

In 1989, Congress changed HMDA to collect data about denied home loan applications and related applicant or borrower information. In 2002, the Federal Reserve Board amended HMDA Regulation C to require new data fields and price information for loans covered by the Home Ownership and Equity Protection Act (HOEPA) including lien status, loan pricing and whether an application or loan involves a manufactured home.[26] The institutions must report the type, purpose, amount of loan; the property's location; and the applicant's ethnicity, income, race and sex. HMDA data includes most home-secured loans, except for home equity loans for credit card debt consolidation or medical expense payments. Regulations make reporting of home equity lines of credit (HELOCs) financing optional.

Effective January 1, 2007, the FRB increased the asset-size exemption for banks, consumer finance companies, credit unions, mortgage companies with offices in metropolitan areas and savings and loan associations. Lenders with $36 million or less on December 31, 2006 do not have to collect or report data under HMDA in 2007.[27]

Home Equity Lines of Credit (HELOC) in Texas

Texas voters authorized two amendments to the Texas Constitution in 2003. The first permitted lenders to provide home equity lines of credit (HELOCs) to Texas homeowners. The second allowed the refinancing of a home equity loan with a reverse mortgage. Interest rates are lower on a HELOC than on unsecured loans from most lenders, and interest paid on a HELOC can be deductible from federal income taxes.[28]

Home equity loan funds may have a value equal to 80 percent of the market value of the home less any loans secured with the home and can be used as needed for any type of expense. A traditional home equity loan is extended for a specific time period with required repayment of interest and principal in equal monthly payments at fixed interest rates. A HELOC is a revolving account that allows the homeowner to borrow from time to time up to a certain credit limit.[29]

The financial services industry, the U.S. Census Bureau and the Federal Reserve Board collect and report HELOC data. Banks and finance companies report HELOCs as receivables on quarterly Call Reports, and mutual savings banks report HELOCs on Federal Reserve Call Reports. Federal savings banks and savings and loan associations report credit line receivables on Call Reports. Finance companies, however, report commercial and residential mortgages without separating HELOCs from traditional loans.[30]

The CRA: Problems and Progress

Opponents and supporters continue to debate the problems and progress created by the CRA. Critics argue that the CRA reduces profits of regulated financial institutions, increases regulatory and reporting burdens and forces banks to make unprofitable high risk loans. Supporters of the CRA point to empirical research showing CRA widened access to credit for low-income, moderate-income and minority borrowers at relatively low cost in the 1990s. These supporters also highlight research showing that for most banks low- and moderate-income home purchase lending has become as profitable as home purchase lending to other income groups.[31] Generally, CRA scholars argue that the CRA encourages lenders to not ration credit in low- and moderate-income communities, where economic activity is often stunted due to relatively low property values, a low volume of comparative property appraisals and reduced liquidity.[32]

When the CRA was passed in 1977, banks and savings and loan institutions issued most home purchase loans. The CRA promoted homeownership lending through access to credit for low- and moderate-income persons by the CRA-regulated institutions in their communities between 1977 and 2005. In the past 30 years, bank activity in low-income communities has grown as CRA regulations changed. For small businesses, CRA advocates suggest progress has been made. However, they recommend further rulemaking and laws to consider the impact of financial services and home mortgage services industry consolidation. CRA supporters argue that small business lending is not repeating the gains made in homeownership lending in low-income areas in the 1990s.

CRA reform advocates urged federal regulators to revise the CRA in 2005. CRA advocates, consumer protection groups and the Consumer Bankers Association among others quickly voiced concerns. They were concerned that regulators' changes to bank size definitions, the new community development test and the reduction of CRA data collection requirements for small and intermediate banks had removed the original reservoir of annual demographic and lending data previously used by consumer protection groups to monitor banks' CRA compliance-related service activities and lending practices. The National Community Reinvestment Coalition argued that the new CRA 2005 rules put the regulated banks' interests above those of the public. On behalf of large banks, the Consumer Bankers Association opposed the size-based bank testing rules arguing that CRA tests should be equally applied to all banks.[33]

Since the 2005 hurricane disasters, CRA advocates have focused their attention on rule changes to the financial industry to stimulate economic activity through community development lending in all areas, not just urban centers. In response, the OTS modified its definition of community development applied to savings associations to conform to that of the FRB, the OCC and the FDIC's final rule of August 2005 that applies to banks. As a result, OTS' April 12, 2006 rule encourages savings associations to increase community development loans and services, and qualified investments in nonmetropolitan middle-income areas and areas affected by disasters.

Small Business, Small Farm and Community Development Lending in the U.S. and Texas

The SBA's Office of Advocacy defines small business as an independent business having fewer than 500 employees. According to the SBA, the U.S. has approximately 26 million small businesses. Nationally, almost 6 million small businesses have employees. Small businesses with fewer than 500 employees represent about 99.7 percent of all employers and generate half of total U.S. non-farm private output and produce 52 percent of private sector output.[34] Small businesses comprise more than 93 percent of businesses in every state and create more than half of all jobs in the U.S. The SBA estimates that small businesses contribute more than 50 percent of non-farm private gross domestic product (GDP), pay 45 percent of total U.S. private payroll and comprise 97 percent of the total number of identified exporters in the U.S. economy.[35]

During the last decade, small firms generated between 60 to 80 percent of the net new jobs annually in the U.S. and employ 41 percent of high tech workers (e.g., scientists, engineers and computer workers).[36] Data from the Federal Procurement Data System – *Next Generation* showed that small businesses received approximately $80 billion in federal contracts in 2005.[37]

Small businesses are a critical component of the economies of both the U.S. and Texas. Research released by the SBA, *Small Business and State Growth: An Econometric Investigation*, found that the start of new small firms is the single most important factor in growing gross state product, state personal income and total state employment.[38] Small firms create the majority of new jobs, increase competition, fuel innovations and fill niche markets.

Across the U.S.

Each year, the FFIEC collects loan data reported by CRA-regulated entities with assets of $250 million or more and institutions of any size if owned by a holding company with assets of $1 billion or more. This includes small business, small farm and community development loan data. The data include information on the number and dollar amount of loans originated or purchased and exclude applications denied by the institution or that do not result in a loan origination. The data excludes information about applicant income, sex, race or ethnicity, but indicate whether a loan is extended to a borrower with annual revenues of $1 million or less. The maximum small business loan size reported is $1 million, and the maximum small farm loan size reported is $500,000.[39]

A total of 1,103 lenders reported CRA data on small business, small farm and community development lending in 2005. This information came from 891 commercial banks and 212 savings institutions. The FFIEC

2005 CRA Data
Loans to Small Businesses and Small Farms in the U.S.
With Revenues of $1 Million or Less
(Lenders Reporting to the FFIEC = 1,103

	Small Businesses	Small Farms
Total Dollars Loaned	$272 Billion	$12.7 Billion
Total Number of Loans	8,000,000	219,000
Average Loan Amount	$34,200	$58,000
Percentage of Loans to Businesses with Less than $1 Million in Revenues	47%	83%
Percentage of Loans Under $100,000	94%	84%
Percentage of Loan Originations and Purchases by Large Commercial Banks & Savings Associations with Assets of $1 Billion or More	90%	>50%

found the average small business loan was approximately $34,200, and the average small farm loan was about $58,000. About 93 percent of the small business loans and 83 percent of the small farm loans were for amounts under $100,000. An estimated $279 billion was loaned through 8 million small business loans, and $17 billion was loaned through 289,000 small farm loans.[40]

Based on the number of loans, the CRA 2005 data indicate 47 percent of the reported number of small business loans and 83 percent of the number of small farm loans were made to businesses with revenues of $1 million or less.

Banks and savings institutions with assets of less than $1 billion were not required to report their 2005 small business and small farm lending due to Office of Thrift Supervision amendments to the CRA regulations in 2004 and amendments by the Office of the Comptroller of the Currency in 2005.

The FFIEC found that 47 percent of small business loans made in 2005 were to small firms, compared to 38 percent in 2004 and a high of 60 percent in 1999. Reduced lending to small businesses may be due to credit card lending to larger firms, changes in bank data collection practices and renewals with higher credit limits. Some small business loans made by banks may go unreported since a number of banks no longer ask for or collect revenue-size data from business loan customers.[41]

The distribution of small business loans for lending reported under the CRA across census tract cities, rural and suburban areas reveals that: 86 percent of the number of small business loans for the reporting period were concentrated in principal city and suburban areas and 60 percent of the small farm loans, measured by the number and dollar amount, were made in rural areas.

The number of community development loans fell from 2004 among the 1,103 reporting CRA institutions 2005. An estimated 74 percent of banks made community development loans and the number of reporting institutions dropped 36 percent to 813 in 2005 from 1,280 in 2004. The reduced loan report figures due to changed CRA rules largely because exempt institutions with assets of less than $1 billion did not have to report loan CRA loan data. Consistent with reporting for 2004, lenders with $1 billion or more in assets made the largest number of community development loans in 2005.[42]

In Texas

Small businesses are the single largest source of new employment growth nationally creating two out of every three new jobs.[43] In Texas, small businesses provide thousands of new jobs for minorities and women.

As of 2005, the SBA Office of Advocacy estimated Texas had an estimated 2 million small businesses based on the U.S. Census Bureau's 2003 percentage of small business multiplied by the total number of employer businesses in 2005 from the U.S. Department of Labor. This figure included the Census Bureau's 2004 number of non-employer firms.

For 2005, the SBA identified more than 400,000 firms with one or more paid employees of which 98.7 percent (407,200) were small firms with fewer than 500 employees. Self-employment fell by 4.8 percent to 1,142,200 in 2005 from 1,200,300 in 2004.

The majority of Texas small businesses fall in the retail and services category with less than $500,000 in annual revenues. Small non-farm businesses showed progress between 2004 and 2005. According to the U.S. Department of Commerce, this sector's business income grew 7.6 percent between 2004 and 2005 to $105.2 billion from $96.2 billion.[44]

In terms of business turnover, the Community Reinvestment in Texas Work Group's research of small businesses for 2005 found that new employer businesses were up 55,858 (3.3 percent) from 2004, business bankruptcies jumped by 3,590 (16.0 percent) in 2005 and business terminations fell to 55,039 (-1.3 percent) in 2005 from 55,461 a year earlier.

Financing of Small Business in the U.S. and Texas

Research published by the SBA since the 2005 update concluded that large lending institutions dominated commercial, industrial and small business lending markets. Small businesses secure funding through combinations of financing methods, mostly small local commercial lenders, debt and equity and deferred capital or funds held until a future date for the business. More than 50 percent of the capital of small businesses in Texas comes from commercial bank loans. Small business start-ups often start with tapped equity of individuals and private firm financing, public nonprofit operations and venture capital entity funding. Generally, venture capitalists are long-term investors, often with specific industry experience, who may "take a hands-on role" with companies they support.[45]

The SBA Office of Advocacy research found that angel investment funds are the largest source for seed and startup venture capital. Generally, angel funds come from affluent individuals or a group of wealthy individuals that supply capital to one or more emerging and innovative businesses. These funds are usually part of the initial or "seed" round of financing an unproven start-up business in generally six month rounds in the range of $1 to $5 million.[46]

Measured by venture capital-backed companies headquartered in the state in 2005, Texas was second only to California in related venture-backed company revenue, in creating jobs nationally and by total venture-backed company employment. In the fourth quarter of 2006, venture capitalists in Texas invested mostly in the equipment and networking, semiconductors and telecommunications industries.[47]

For traditional bank financing of small businesses, SBA Office of Advocacy statistics for 2005 show that large banks issued 39 percent of small business loans under $1 million while small businesses were awarded $79.6 billion in federal contracts in 2005. Between June 2004 and June 2005, the total number of small business loans grew 22.6 percent. The SBA's data show a total of more than $600 billion in the form of 21 million small business loans in June 2005, compared with 17 million loans totaling $577 billion in June 2004. Loans under $100,000 increased most, leaping to $19 million in 2005 from just over $15 million in 2004. Business credit cards loans accounted for 70 percent of the loans under $100,000 in 2005.[48] In June 2005, total small business loans under $1 million amounted to $600 million out of the $1.68 trillion in total business loans issued.

Commercial banks provide more than 80 percent of credit line loans for small businesses. With the exception of the lease market, these banks supply more than 50 percent of the commercial mortgages, equipment, vehicle and other loans. In Texas, both commercial banks and savings and loan institutions make loans to small businesses.

Small business loans made by finance companies increased since 2001 across the U.S., rising 3.2 percent in 2004 alone. Between June 2004 and June 2005, venture capital financing totaled $22 billion, and angel investments grew to $23 billion. Alone, early-stage and seed financing by venture capital companies totaled $4.1 billion in 2005.[49] Because of their economic importance, banking analysts, legislative affairs groups, state and federal regulatory agencies and small business advocates continue to examine the factors affecting small business growth and access to capital and credit. A crucial component of small business funding involves community redevelopment business lending.

Community Development Lending Across the U.S. and Texas

By definition under the CRA, community development loans provide support primarily for affordable housing for low- or moderate-income persons and community services for these populations including activities that encourage economic development through small business or small farm loans. Community Development Corporations (CDCs) and Community Development Financial Institutions (CDFIs) use community development loans to revitalize low- and moderate-income communities.

New Definition of Community Development Helps Rural Areas

Federal banking and thrift regulatory agencies revised CRA regulations in 2005 and 2006 following devastation of the U.S. Gulf Coast left by Hurricanes Katrina and Rita. Revitalization or stabilization activities must help one or more of the following CRA populations: distressed or underserved non-metropolitan middle-income geographies based on two criteria sets, e.g., rates of poverty and loss of employment, population and density.

Changes to the CRA's community development definition and criteria in 2005 and 2006 allow the award of CRA credit to national banks that invest in and fund rebuilding communities in and outside of their assessment areas affected by either of the two hurricanes. National banks may also receive CRA credit for supporting community reinvestment efforts in rural areas and funding bank activities that stabilize or stimulate federally-designated disaster areas. Designated disaster areas are major federal government-determined disaster areas administered by the Federal Emergency Management Agency (FEMA). Examples of CRA-related community development activities include affordable housing for low- and moderate-income persons; bank financing for a new septic line for low- and middle-income individuals; community services for low- or moderate income persons; disaster recovery to preserve existing businesses and attract new businesses and residents and financing of small business or small farm activities that stimulate designated disaster areas, defined non-metropolitan, middle-income geographies that are also underserved or distressed.[50]

The Office of Rural and Community Affairs (ORCA) and the Texas Community Development Block Grant Program (TxCDBG)

In Texas, several agencies have responsibility for community and economic development programs and initiatives. The 77th Texas Legislature created the Office of Rural Community Affairs (ORCA) in 2001 to serve as the state's central agency focusing on the state's rural health, economic development and community development programs. The agency also monitors government actions that affect rural Texas.

ORCA researches rural issues, recommends solutions and coordinates rural programs among state agencies. The agency is composed of the program compliance and audit unit; the research, policy and development unit; the community development block grant program unit; and the rural health unit.

The Texas Community Development Block Grant Program (TxCDBG), managed by ORCA, is the largest community development program in the United States. The Department of Housing and Urban Development (HUD) awarded the program $73,297,579 for program year 2006. The program serves 1,017 eligible rural communities, 245 rural counties and provides services to more than 377,000 people each year.[51]

The TxCDBG Program focuses on providing basic human needs and sanitary infrastructure to small, rural communities in outlying areas. Local needs that are eligible for financial assistance include clean drinking water, sanitary sewer systems, disaster relief and urgently needed projects, housing, drainage and flood control, navigable streets, economic development, community centers and other related activities.

The primary objective of the TxCDBG Program is to develop viable communities by providing decent housing, suitable living environments and expanding economic opportunities. The table below identifies the amounts and purposes of funds administered by the TxCDBG Program.

Every biennium, eligible cities and counties may apply through a regional competition for Community Development Fund assistance. Eligible activities include infrastructure projects such as drainage, sewer and water system improvements, housing rehabilitation, and improvements to bridges and streets. Each of the 24 state planning regions receives an allocation each year based on population, poverty and unemployment levels.

Recognizing the importance of participation by local jurisdictions, ORCA and Regional Review Committees (RRC) share the process of scoring applications for these funds. Each Regional Council of Government has its own RRC composed of 12 local officials appointed by

Texas Community Development Program
2006 Funding Summary

Fund	Amount
Community Development Fund	$41,596,376
Community Development Supplemental	$3,188,445
Non-Border Colonia (NBC) Fund	$0.00[1]
Texas Capital Fund	$10,635,478
Colonia Construction Fund	$5,211,458
Colonia Economically Distressed Areas Program (EDAP) Fund	$1,781,131
Colonia Planning Fund	$337,169
Colonia Self-Help Centers Fund	$1,832,439
Disaster Relief/Urgent Need Fund	$3,452,316
Planning and Capacity Building Fund	$659,678
Microenterprise Loan Program[1]	$1,000,000[2]
Small Business Loan Program[1]	$1,000,000[2]
Section 108 Loan Guarantee Pilot Program[2]	$500.00[3]
STEP Fund (Small Towns Env. Program)	$2,316,204

Source: Office of Rural and Community Affairs, September 2006.
[1]All 2006 applicants were funded in 2005 using de-obligated funds (returned funds to ORCA previously awarded) and / or program income.
[2]Program Income of up to $1,000,000 is available.
[3]Up to $500,000 in loan guarantee commitments are available.

the governor for two-year staggered terms. The RRCs' role is to help determine regional priorities for projects funded through Community Development Fund and the Community Development Supplemental Fund administered by ORCA. RRCs also develop the scoring criteria for three categories: local effort, project merits and priorities. The RRCs hold meetings in each of the 24 regions to score applications. RRC scores account for 50 percent of the total score, while ORCA scores provide the other 50 percent.

The Small Towns Environment Program (STEP) is a community development fund that encourages the community's residents to help themselves by committing local volunteers, donating their own money and providing available construction materials for the construction, operation and maintenance of water or sewer projects and services.

ORCA, recognizing that successful community development encompasses strategic community planning that incorporates all facets of Texas localities, offers the Planning and Capacity Building Fund. This fund provides assistance for planning activities to assess local needs, develop strategies to address local needs, build or improve local capacity or develop comprehensive plan-related elements.

ORCA offers a separate Colonia Planning Fund on an annual basis to eligible counties located within 150 miles of the Texas-Mexico border. Similar to the Planning and Capacity Building Fund, this fund also provides assistance for planning activities that assess local needs, develop strategies to address local needs and build or improve local capacity.

While the agency focuses its efforts on all eligible rural communities statewide, several funds are directed to a much narrower target audience, the colonias. These funds include the Colonia Construction Fund, Non-Border Colonia Fund, Colonia Economically Distressed Areas Program Fund and the Colonia Self-Help Centers Fund.

The Colonia Construction Fund provides assistance to those colonias located within 150 miles of the Texas-Mexico border, while the Non-Border Colonia Fund provides funding for colonias throughout the remainder of the eligible counties in Texas. These two funds are primarily used to construct safe, sanitary, and cost-effective water and sewer facilities for colonias that lack such infrastructure.

The Colonia Economically Distressed Areas Program Fund is used to provide assistance to colonia areas connecting to a Texas Water Development Board Economically Distressed Areas Program (TWDB EDAP)-funded water and sewer system improvement project.

The Colonia Self-Help Centers Fund is designed to assist individuals and families of low-income and very low-income to finance, refinance, construct, improve or maintain a safe, suitable home in the colonias' designated service area or in another area that has been determined is suitable.

ORCA identifies new tools and opportunities to assist rural Texas with economic development to create balanced and viable communities, such as the Microenterprise Loan Program, which awards between $50,000 and $100,000 to eligible cities and counties for loans to commercial enterprises with five or fewer employees. The Small Business Loan Program provides similar compensation to eligible cities and counties for loans to businesses with 100 or fewer employees.

ORCA also provides assistance to rural Texas through its Rural Health Division. ORCA Rural Health's mission is to facilitate and coordinate the use of available resources to help rural Texans enhance their quality of life, achieve sustained economic growth and strengthen local healthcare infrastructure and systems of care to better meet the needs, challenges and priorities of rural Texas. The Rural Health Division works closely with many local, state and federal partners to develop, support and coordinate programs and services to assist rural Texas communities in improving access to quality health services across the continuum of care that meet local needs. This division of ORCA also informs, guides and facilitates efforts in rural health policy design, service planning, resource allocation and program implementation.

ORCA approves financial support for disaster relief and to meet urgent needs if the situation addressed by the applicant was unanticipated and beyond the control of the local government. It also can approve financial support if the problem 1) occurred no more than 18 months before the submission of an application for TxCDBG Program assistance or b) when the applicant demonstrates that local funds or funds from federal sources or another state source are not available to adequately address the problem. The TxCDBG Program coordinates distribution of funds with other state agencies.

Disaster Relief funds help communities on an as-needed basis to recover from natural disasters, drought, flooding or tornadoes when the governor has proclaimed a state disaster or has requested a federal disaster declaration. TxCDBG Program funds are used to restore basic housing, water and sewer facilities.

ORCA supplies money from several funds to eligible county applicants for projects in economically depressed unincorporated residential areas along the Texas-Mexico border known as colonias. According to the Texas Secretary of State, about 400,000 Texans live in colonias, which lack electricity, adequate sewage systems and decent, safe and sanitary housing.

ORCA Activities for Hurricanes Katrina and Rita

Under the revised CRA definition of community development, disaster relief funds became eligible for non-housing related activities. Designated Councils of Governments (COGs), whose service areas contain the overlapping 29 counties eligible for the Federal Emergency Management Agency (FEMA) Public Assistance program as well as cities, counties and federally recognized Indian Tribes, may apply for funds through ORCA.[52] Individual contracts will be prepared between the State and each county and city that receives grant awards. A grantee may also have the COG arrange for local grant administration.

Estimate of Damages

According to FEMA and the Governor's Division of Emergency Management, the most current estimate of damage to Texas infrastructure caused by Hurricane Rita is $385.8 million as of November 16, 2006. Schools, hospitals, critical private nonprofit organizations, local jurisdictions and utilities are among those that sustained financially crippling damages.

Non-Housing Activities

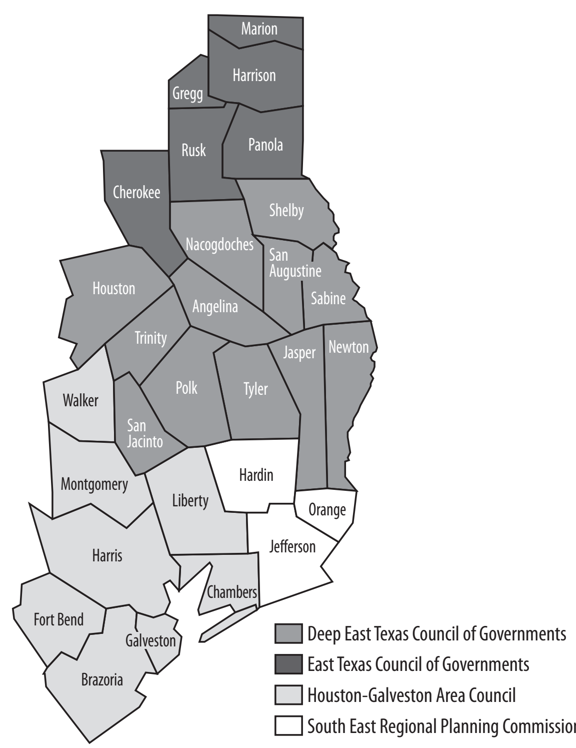
ORCA's Non-Housing activities include, but are not limited to, the FEMA Infrastructure Grant Program match, the FEMA Hazard Mitigation Grant Program match for drainage projects, flood buyouts in which the property is converted into open, undeveloped land, and safe-room and community storm shelters, the Natural Resource and Conservation Service (NRCS-USDA) flood and drainage projects, roads and bridges, water control facilities, water and waste water facilities, buildings and equipment, hospitals and other medical facilities, utilities, parks and recreational facilities, debris removal, public/community shelters and loan funds for businesses. All of these non-housing activities must be related to addressing damages created by Hurricane Rita.

CDBG Disaster Recovery Funds

The Governor selected the Texas Department of Housing and Community Affairs (TDHCA) and the Office of Rural Community Affairs (ORCA) to administer $74,523,000 in federal Community Development Block

Counties Eligible for Hurricane Rita Disaster Recovery Assistance

Angelina	Houston	Polk
Brazoria	Jasper	Rusk
Chambers	Jefferson	Sabine
Cherokee	Liberty	San Augustine
Fort Bend	Marion	San Jacinto
Galveston	Montgomery	Shelby
Gregg	Nacogdoches	Trinity
Hardin	Newton	Tyler
Harris	Orange	Walker
Harrison	Panola	



Grant (CDBG) funding for housing, infrastructure, public service, public facility and business needs in the 29-county area directly impacted by Hurricane Rita. These funds are intended to assist with long-term recovery efforts and infrastructure restoration in the four COG areas including the East Texas Council of Governments (ETCOG), Deep East Texas Council of Governments (DETCOG), Southeast Texas Council of Governments (SETCOG), Houston-Galveston Area Council (H-GAC), with TDHCA administering approximately 56.9 percent of the funds for housing and public services and ORCA, approximately 43.1 percent of the funds for public infrastructure, public facilities and business needs.

Funding Allocation

Housing Activities – $40,259,276
Non-Housing Activities – $30,537,574
Administrative Fees (5 percent) – $3,726,150
Total Distribution = $70,796,850
Total (Including 5 percent in fees) = $74,523,000

Rural Health Disaster Relief & Recovery Grant

ORCA established through its Rural Health Division a Rural Health Disaster Relief & Recovery Grant to help rural hospitals and rural health clinics respond to a federal or state disaster declaration. The funds could only be used for relief efforts in response to or recovery from a natural disaster event.

ORCA administered another 18 Hurricane Katrina relief projects funded in Orange, Anahuac (2), Jasper (4), Kirbyville (2), Rayburn, Buna, Marshall, Henderson (2), Newton, Liberty, Hemphill and Winnie, for a total of $400,208.

Funds Distributed Among the Four COG Areas Based on the Greatest Documented Need and the Most Identified Distressed Areas

COG Region	Housing Allocation	Non-Housing Allocation	Total Allocation	Percent (%) of Total
SETRPC 3 Counties	$26,498,536	$12,468,656	$38,967,192	55%
DETCOG 12 Counties	$ 6,745,034	$12,278,209	$19,023,243	27%
H-GAC 8 Counties	$ 7,015,706	$ 3,690,712	$10,706,418	15%
ETCOG 6 Counties	$0.00	$ 2,099,997	$ 2,099,997	3%
TOTAL	$40,259,276	$30,537,574	$70,796,850	100%

Disaster Funds Distributed By ORCA In 2005

Bonham	$50,000	Repair portions of Bonham Civic Center roof to house evacuees.
Crockett	$50,000	Install additional showers, laundry facilities and a generator.
Jasper	$50,000	Rehabilitate Community Church of Jasper's kitchen facilities.
Jefferson Co.	$50,000	Purchase chairs, tables and disaster supplies for Ford Park Complex.
Nacogdoches	$30,000	Improvements to C.L. Simon Recreation Center's HVAC system.
West Orange	$50,000	Rehabilitate and expand restrooms and kitchen at Stark ISD School.
Browndell	$50,000	Rehabilitate restrooms, kitchen and repair roof at Community Center.
Subtotal	**330,000**	Public Shelter Improvements only (Katrina).
Browndell	$50,000	Expand capacity of public shelter (Rita and Katrina).
Hemphill	$50,000	Expand capacity of public shelter (Rita and Katrina).
Total	**$430,000**	**Disaster Funds Distributed by ORCA in 2005**

Community Reinvestment and State Agency Programs

Banking

The Texas banking industry has undergone significant changes over the last 25 years. In the 1980s and early 1990s, a number of banks and savings institutions failed under what some analysts characterized as the financial equivalent of the "perfect storm." The ingredients of this financial catastrophe included economic instability, changes in tax law for real estate investments, a dramatic fall in crude oil prices, high inflation, excessive leverage, disproportionate lending concentrations, deregulation and fraud and insider abuse.

During this period, market interest rates increased dramatically. Savings institutions that held large volumes of fixed rate mortgages suffered an erosion of their net interest margins. In the aftermath of this upheaval, many Texas-based institutions were left in a weakened condition. Interstate banking that began in Texas in 1987 allowed out-of-state holding companies to enter Texas and infuse much-needed capital into these troubled institutions through mergers and acquisitions.

While the Texas economy recovered from these harmful conditions, the trend of mergers and acquisitions in the banking industry continues, most pronounced among the larger multi-state institutions. In 2006, large multi-state operations controlled $221 billion, more than half, of $402 billion in deposits in banks in Texas. Small locally-owned banks control a higher percent of the market in smaller communities. A large number of out-of-state banks are conducting business in Texas, and the Texas Department of Banking expects this trend to continue.

The number of out-of-state banks and thrifts, both state and national charters conducting business in Texas, has increased by more than 50 percent in the last five years, increasing from 24 on June 30, 2001 to 38 at year-end 2006. As markets in other states approach saturation, the vibrant and diversified economy of Texas will attract other out-of-state financial institutions.

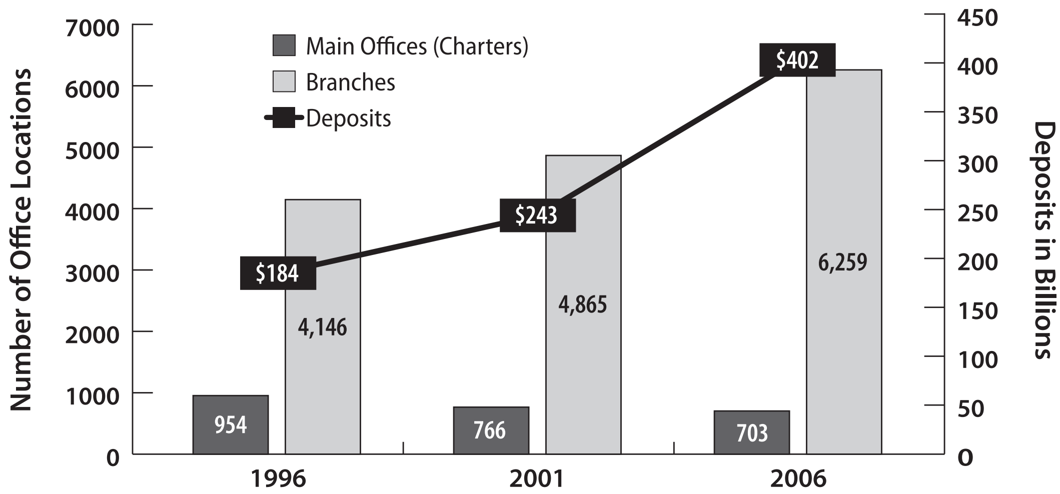
In the last 10 years, mergers and acquisitions have resulted in fewer financial institution charters, which are the main bank offices or bank headquarters. The trend in Texas is that fewer charters are issued, while remaining banks continue to expand operations by building new branches to meet the customers' need for convenience. The number of charters for banks and savings institutions decreased 26 percent from 954 in 1996 to 703 in 2006. Improving economic conditions in Texas and a favorable banking climate encourage the "branch building" trend. Texas branches increased 51 percent between 1996 and 2006, growing from 4,146 to 6,259 branches. The following table "Offices and Deposits of Depository Institutions Operating in Texas," depicts the number of office locations, branches and deposits as of June 30 of 1996, 2001 and 2006.

Due in part to the robust Texas economy and the trend toward more branch locations, the deposits controlled by the remaining banks and savings institutions increased over the last five years, from $243 billion in 2001 to $402 billion in 2006. The average asset of financial institutions in Texas, excluding credit unions, was $271 million at the end of 2006, compared with $248 million at the end of 2005. Out-of-state, state-chartered banks' total assets reached $16.3 billion in 2006. The sum of all assets of state-chartered deposit institutions, excluding credit unions, equaled nearly $110 billion in 2006.

Given the positive estimates for both job and population growth for the next five years, the Texas Department of Banking anticipates that banks and savings institutions will continue to establish new branches, and the average bank size is expected to increase. Industry executives, previously displaced when their employer institutions were sold, are entering into ventures to charter new financial institutions.

The Texas banking environment outlook is favorable for the remainder of 2007, following a year of excellent financial performance of Texas' commercial banks and savings institutions. Factors supporting the banking industry included an improving and healthy economy, robust consumer spending and strong housing and construction markets. While the state's housing market has escaped the weakening found in other states, recent statistics reflect that single-family building permits and new house construction have decreased.

Offices and Deposits of Depository Institutions Operating in Texas



Despite a flattening of the yield curve, the financial industry in Texas has been able to maintain its margin. Financial institutions traditionally rely upon earning the spread between longer term assets funded by short-term deposit liabilities. In 2006, the yield curve became inverted, meaning that short-term rates exceeded long-term rates. Typically, this causes a narrowing of financial institutions' net interest margins. In the second half of 2006, this became apparent as many banks saw a reduction in their net interest margins.

The Texas Department of Banking expects overall performance for banks and thrifts to be favorable through 2007 due to the renewed strength of the Texas economy in 2005 and 2006. Bank and thrift managers must manage their interest rate risk during a rising rate environment or suffer deterioration in their net interest margin. This would be necessary if higher gasoline prices persist into 2008. Combined with an escalating amount of consumer debt and delinquencies in the subprime mortgage loan market, consumer confidence may drop and depress consumer spending and home sales.[53]

Banking contributions to the Texas economy are vital to stimulating opportunities to small businesses and entrepreneurs. Capital loans to small businesses by banks fuel employment opportunities for Texans. The Texas Department of Banking assesses how well banks are meeting the needs of their communities through funding of affordable housing projects, loans to low- and moderate-income businesses and individuals and projects compliant with the CRA. The agency follows up on the reported CRA performance of the banks it oversees and the findings of CRA examinations. The agency also provides consumer assistance through its Web site, the agency's consumer complaint section and periodic agency publications.

The Finance Commission of Texas serves as the statutory oversight body for the Texas Department of Banking, the Texas Department of Savings and Mortgage Lending and the OCC. Under section 11.305 of the Texas Finance Code, it is the responsibility of the banking commissioner, savings and mortgage lending commissioner or consumer credit commissioner to research the availability, quality and prices of financial services, lending and depository services and the practices of business entities in the state that supply financial services to agricultural businesses, small businesses and individual consumers. In December 2006, the Finance Commission conducted a financial services study.

Economic Development

The Texas Economic Development and Tourism Division (EDT) is part of the Office of the Governor. Senate Bill 275 of the 78th Legislature transferred the functions of the Texas Department of Economic Development to the Governor's office and created the Economic Development Bank within EDT by combining finance programs previously administered by the Department. The finance programs include the Texas Small Business Industrial Development Corporation, the Industrial Revenue Bond Program established under the Development Corporation Act of 1979 (Article 5190.6, Vernon's Texas Civil Statutes), the Texas Enterprise Fund established under S.B. 1771, the Product Development Fund and the Small Business Incubator Fund established under Government Code, Chapter 489, Subchapter D.

The EDT works with companies seeking to expand or relocate into Texas communities and administers programs that encourage the financing of local economic development projects. These include the Capital Access Program (CAP) and the Texas Linked Deposit Program. The Governor's Small Business Assistance team provides additional help, information and support for communities and businesses.

Created by the 75th Legislature in 1997, the CAP is a public/private partnership between the Texas state government and lending institutions that allows eligible businesses to access needed capital for start-up or expansion. The chart below shows the CAP transaction history from fiscal 2001 through fiscal 2005 (funding was not available in 2006).

The Linked Deposit Program is a partnership between the EDT, the Comptroller's office and approved depository lenders that encourages lending to minority and women-owned businesses, child-care centers, non-profit organizations and small businesses located in state-designated enterprise zones. Loans range from $10,000 to $250,000 and can be used as working capital and for the lease, purchase or construction of capital assets such as land, building and equipment. Since 1995, the Linked Deposit Program has participated in creating 63 new jobs and retaining 199 jobs in Texas.

The Small Business Assistance section of the EDT serves as the principal focal point in the state to assist small and historically underutilized businesses. The program represents the Governor's Office as an advocate for small business issues affecting the state of Texas.

Starting in fiscal 2005 and continuing into fiscal 2006, Small Business Assistance provided support to the Governor's Small Business Economic Development Summits held in El Paso, San Antonio, Edinburg, Tyler, Houston, Lubbock and College Station with more planned for fiscal 2007. The summits discussed obtaining financing from a variety of sources, opportunities for exporting, developing the work force, taxes and tax credits, starting your own small business, doing business with the state and providing employee health care.

The summits identified sources of financing for start-up and expanding businesses including conventional lenders, the Small Business Administration (SBA), community development corporations and non-profit community micro-lenders (community development financial institutions). Representatives of each group presented a short seminar on how to obtain financing and were available during a "Meet the Lender" session. The summits also provided information on loan requirements of lenders and afforded small businesses the opportunity to make direct contact with various lenders.

Housing

A number of housing programs encourage community reinvestment in Texas. The programs provide down-payment assistance, low-interest rate loans or subsidies for the acquisition, development or rehabilitation of both single-family and multifamily housing.

The Texas Department of Housing and Community Affairs (TDHCA), the state's lead agency for affordable housing and community assistance programs, annually administers funds of more than $400 million. The majority of TDHCA housing program funds are federal

Capital Access Program Loans: 2001-2005

	2001	2002	2003	2004	2005
Loans Enrolled	395	421	184	310	195
Amount Enrolled	$15,674,027	$10,136,574	$2,063,206	$5,273,692	$3,295,158
Total Investment	$21,139,379	$17,237,719	$2,607,077	$9,406,617	$10,801,801
State's Participation	$718,549	$481,840	$116,429	$360,151	$227,152
Average Loan Size	$53,517	$40,945	$11,213	$17,012	$16,898
Participating Lenders	9	13	7	8	6
Jobs	2,987	2,202	N/A	N/A	N/A
Leverage Ratio	29:1	36:1	22:1	26:1	47:1
Cities	96	106	62	65	53

Source: Economic Development and Tourism Division, Office of the Governor.

grants and tax credits combined with money derived from mortgage revenue bond financing. Ninety-two percent of the households served by TDHCA housing programs in fiscal 2005 were low-income at or below 80 percent of the area median family income (AMFI).

TDHCA's housing programs also help fuel the Texas economy. For example, the National Association of Home Builders (NAHB) reported that building 100 single-family units generates 347 jobs and $19 million in new income in the state.[54] Several TDHCA programs support and encourage community reinvestment.

The Single-Family Bond Program, funded from tax-exempt and taxable mortgage revenue bonds, assists low- to moderate-income Texas residents with the purchase of their first home or those who have not owned a home during the past three years. Participating lenders must complete a Mortgage Lender Questionnaire that asks for the institution's current rating under the CRA, although this is not a requirement for participation. TDHCA does not require the CRA rating because it does not seek to restrict participation in the program by interested lenders.

Each year, TDHCA sets aside 20 percent of the funds in the Single-Family Bond Program for one year to encourage participation in areas most needing community reinvestment. TDHCA applies these funds toward loans in areas of chronic economic distress. At the end of the fiscal year, remaining funds may be used to purchase homes in non-targeted areas. In fiscal 2005, the program allocated a total of about $210 million and served 2,384 families. About 78 percent of those served had incomes below 80 percent of the area median family income (AMFI).

The program includes three activities. The Texas First-Time Homebuyer Program channels below-market interest rate mortgage money through participating Texas lending institutions to eligible families. Although income limits may vary with each bond issue, the program is designed to serve families with income ranging from 30 to 115 percent of AMFI. The American Dream Downpayment Initiative (ADDI), effective December 16, 2003, assists homebuyers with down payment and closing costs. ADDI aims to increase the homeownership rate, especially among lower income and minority households, and revitalize and stabilize communities. Under ADDI, a first-time homebuyer must not have owned a home during the three year period prior to the purchase of a home with assistance under ADDI. The initiative also helps displaced homemakers and single parents. ADDI assistance provided to any family may not exceed the greater of 6 percent of the purchase price of a single-family housing unit or $10,000 and is in the form of a second- or third-lien loan. The Down Payment Assistance Program (DPAP) helps low-income families purchase homes with interest-free loans ranging from $5,000 to $10,000, depending on the county where the property is located. The assistance is used as a down payment or to cover eligible closing costs. The borrower repays the loan when the original mortgage matures or when the home is either refinanced or sold.

The Grant Assistance Program (GAP) provides up to 4 percent of the loan amount for the down payment and closing cost assistance. The funds are available on a first-come, first-served basis for mortgage loans originated through the First Time Homebuyer Program. Assistance is available to eligible borrowers whose incomes do not exceed 60 percent of AMFI.

The Mortgage Credit Certificate (MCC) program provides a tax credit that will reduce the federal income taxes, dollar-for-dollar, of qualified buyers purchasing a qualified residence. The MCC reduces the monthly mortgage payment and increases the buyer's disposable income by reducing his or her federal income tax obligation. This tax savings provides a family with more available income to qualify for a loan and meet mortgage payment requirements. The amount of the annual tax credit will equal 35 percent of the annual interest paid on a mortgage loan. The maximum amount of the credit cannot exceed $2,000 per year and cannot be greater than the annual federal income tax liability, after all other credits and deductions are considered. MCC tax credits in excess of a borrower's current year tax liability may be carried forward for use during the subsequent three years. The MCC Program provides homeownership opportunities for qualified individuals and families whose gross annual household income does not exceed 115 percent of AMFI limitations, based on IRS adjusted income limits. To participate in the MCC Program, homebuyers must meet certain eligibility requirements and obtain a mortgage loan through a participating lender. The mortgage loan must be financed from sources other than tax-exempt revenue bonds. The mortgage may be a conventional, Federal Housing Administration (FHA), Department of Veterans Affairs (VA) or Rural Housing Services (RHS) loan at prevailing market rates, but may not be used in connection with the refinancing of an existing loan.

TDHCA's Multifamily Mortgage Revenue Bond Program issues mortgage revenue bonds to finance loans for qualified nonprofit organizations and for-profit developers. Financed properties must meet what are known as "unit set-aside restrictions" to assist low-income tenants and may include rent limitations and other requirements set by TDHCA. Project developers may elect to set aside 20 percent of the units for households earning 50 percent or less than the area median income; or 40 percent of the units for households earning 60 percent or less than the area median income.

For developments financed under the 501(c)(3) tax-exempt Multifamily Revenue Bond Program, 75 percent must be occupied by households that are at or below 80 percent of the AMFI.[55] Five percent of the units are reserved for special-needs tenants. In fiscal 2005, a total of about $200 million was committed, and 3,288 affordable multifamily apartments were produced.

The Housing Tax Credit Program gives developers of low-income rental housing a tax credit to offset a portion of their federal tax liability in exchange for building affordable rental housing. Nearly $76 million in funds were committed in fiscal 2005 by TDHCA, creating a total of 18,350 housing units for persons at or below 60 percent of median family income. To qualify for the tax credit, 20 percent or more of the project's units must be rent-restricted and occupied by individuals whose income is 50 percent or less than the median family income. Forty percent or more of the units must be rent-restricted and occupied by individuals whose income is 60 percent or less than the median family income.

The HOME Investment Partnerships Program offers grants and loans to local governments, nonprofit agencies, for-profit entities and public housing agencies to provide safe, decent, affordable housing to low-income families. *HOME* allocates funds through Homebuyer Assistance, Rental Housing Development, Rental Housing Preservation, Owner-Occupied Housing Assistance and Tenant-Based Rental Assistance programs. The *HOME* program has a 15 percent set-aside for community housing development organizations and a 5 percent set-aside for those with special needs, including the homeless, the elderly, persons with disabilities, residents of colonias, victims of domestic violence, persons with alcohol or drug dependencies, migrant workers and persons with *HIV/AIDS*. A total of about $47 million was committed in fiscal 2005, serving a total of 2,253 households.

The Housing Trust Fund is the only state-authorized program dedicated to increasing the state's supply of affordable housing. The program' funds are legislatively authorized and competitively award by TDHCA to nonprofit and for-profit organizations, local governments, public housing authorities, community housing development organizations and income-eligible individuals and families for the acquisition, rehabilitation and new construction of affordable housing. Up to 10 percent of Housing Trust Fund annual allocations can be used to train staff and purchase computers. The Pre-Development Revolving Loan Program can also use up to 10 percent of the trust fund allocation to eliminate the barriers that predevelopment expenses, including architect and engineering fees, pose to housing development. About $6 million was committed in fiscal 2005, serving a total of 1,149 households.

TDHCA's *Contract for Deed (CFD) Conversion Initiative* assists residents of colonias, which are unincorporated communities often characterized by poverty, sub-standard housing and inadequate basic services within 150 miles of the Texas-Mexico border. The 76th Legislature in 1999 enacted Senate Bill 867, that creates a guaranteed loan fund to encourage more private lenders to participate in converting CFDs into traditional notes and deeds of trust so that colonia residents build equity in their homes.

The 78th Legislature passed a legislative directive (House Bill 1, 78th Legislature, R.S., Article VII-13, Rider 10) instructing the department to spend at least $4 million on contract for deed conversions for families that reside in a colonia and earn 60 percent or less than the AMFI. Rider 10 also directed TDHCA to convert no less than 400 contracts for deed into traditional notes and deeds of trust by August 31, 2005.

The program helps colonia residents become property owners by converting their contracts for deed into traditional mortgages allowing colonia residents to build equity in their homes. Since the program started in 1999, more than $12.6 million has been committed and more than 620 contracts for deeds converted.

Housing Programs Fiscal 2005

Program	Amount Committed
Single Family Bond Program	$210 million
Multifamily Mortgage Revenue Bond Program	$200 million
Housing Tax Credit Program	$76 million
Home Investment Partnerships Program	$47 million
Housing Trust Fund	$6 million
Contract for Deed (CFD) Conversion Initiative	$2 million
Texas Bootstrap Loan Program	$3 million

Source: Texas Department of Housing and Community Affairs.

The “Bootstrap” Homebuilder Loan Program became law during the 1999 legislative session. The program requires TDHCA to establish a statewide loan program, working through certified nonprofit organizations to enable owner-builders to purchase real estate, construct or renovate a home. The 77th Legislature amended and continued this program under Senate Bill 322 (2001).

Currently, the Texas Bootstrap Loan Program promotes homeownership for low-income Texans by providing funds to purchase or refinance real property on which to build new residential housing, construct new residential housing or improve existing residential housing throughout Texas. Participating owner-builders must provide a minimum of 60 percent of the labor required to build or rehabilitate the home. SB 322 also removed the requirement that the owner-builder must reside with two other family members and increased the loan amount to $30,000. Total loans from the TDHCA and from other entities cannot exceed $60,000 per unit. The department continues its commitment to this program with $6 million over the biennium (fiscal 2006-07) to implement this initiative.

A growing number of lenders and affordable housing professionals recognize that it takes more than flexible underwriting in lending to expand homeownership for low- and moderate-income households. Counseling on the requirements and opportunities of homeownership may reduce mortgage delinquency and foreclosure rates and thereby enhance the availability and soundness of loans made to first-time buyers. TDHCA believes that homebuyer education and counseling can provide lenders, borrowers and policy-makers with the skills and confidence to make full use of the department’s lending programs.

Accordingly, TDHCA created the Texas Statewide Homebuyer Education Program (TSHEP) in 1999. The program provides homebuyer counseling through experienced homebuyer education providers, nonprofit housing providers, low-income housing advocates, for-profit housing providers, lenders and realtors. To ensure a uniform quality of homebuyer education throughout the state, TDHCA contracted with the Neighborhood Reinvestment Corporation to teach local nonprofit organizations the principles and applications of comprehensive pre- and post-purchase homebuyer education and to certify participants as educational providers. During fiscal 2005, TDHCA helped facilitate more than 1,500 homebuyer education courses statewide. Since the program started in 1999, nearly 530 individuals have attended and received certification as trainers.

Insurance

The Texas Department of Insurance (TDI) regulates insurance policies and rates in Texas. It also provides consumer protection services and supervises an estimated 2,000 insurers, health maintenance organizations and continuing-care retirement communities. Annual statements filed by insurers and Health Maintenance Organizations (HMOs) for calendar year 2005 reported $78.7 billion in Texas premiums and $55.3 billion in payments to Texas claimants. These companies reported aggregate assets of $5.8 trillion, liabilities of $5.1 trillion and capital and surplus of $747.1 billion.

TDI’s 2006 biennial report of Texas investments by life and health insurance companies with Texas premiums of $10 million or more shows investments of almost $45.6 billion in 2005 for the 262 insurance companies included in the report. These companies account for almost 98 percent of $31 billion of Texas life and annuity premiums collected in calendar year 2005. The reported Texas investments are not comprehensive since many of the companies’ investments cannot be linked to an individual state. This is particularly the case with pooled investments.

Ninety-three percent of reported investments were in political subdivision/public utility bonds, commercial mortgages and corporate bonds. The largest categories of investments were investments in political subdivision/public utility bonds ($16.4 billion), commercial mortgages (almost $15.6 billion) and corporate bond investments (almost $10.4 billion). Due to the difficulty in linking some corporate bond investments to specific states, reporting for that category was optional, while reporting investments in political subdivision/public utility bonds and commercial mortgages was mandatory for the companies meeting the reporting criteria.

Insurance company residential mortgage investments are frequently made through pooled investments, so comprehensive data was not available for this category. Reporting companies, however, identified almost $382 million in Texas residential mortgage investments. For additional information these investments, see the *December 2006 Community Investment Report* available on the TDI Web site.

Property insurance company investments are not included in the *December 2006 Community Investment Report* since property insurance availability is a key to homeownership for millions of Texans. Homeowner’s insurance is required on all properties that carry liens, so a shortage of available insurance can have a direct effect on a person’s ability to purchase a property. TDI is concerned with ensuring that homeowner's insurance is available. In addition to implementing the Fair Access to Insurance Requirements (FAIR) Plan, TDI and the Legislature have worked together to expand coverage options.

In 2003, the 78th Legislature enacted Senate Bill 14 in 2003 due to concerns over the availability and affordability of insurance. S.B. 14 required insurers to charge rates that are just, fair, reasonable, adequate, not confiscatory, not excessive and not unfairly discriminatory. For the first time in Texas history, all companies writing homeowners insurance are subject to the same rate standards. Before S.B. 14, 95 percent of homeowners' insurers were exempted from rate regulation. SB 14 also:

- created standards to determine whether an insurer's rate is excessive, inadequate or unfairly discriminatory;
- made insurance rate filings public information, prohibited insurers from using a rate until approved by the Texas Insurance Commissioner, required insurers to refund policyholders the difference in an overcharged premium with interest and sent policyholders a written notice of a rate increase to exceed 10 percent of the current policy;
- authorized the TDI to regulate policy forms and endorsements for personal automobile insurance and residential property insurance;
- made amendments to prohibit insurers from using a credit score that is computed using discriminatory factors, e.g., absence of credit information or lack of a credit card account; and
- strengthened TDI's rulemaking powers by authorizing the commissioner to adopt any rules necessary and appropriate to implement the powers and duties of the agency.

CRA and the Insurance Industry

Several differences between the banking and insurance industries are worth noting. For example, a bank's fundamental purpose is to make loans, while an insurance company exists primarily to insure risks and pay claims. While insurers make investments, these are specifically designed to ensure funds are available to pay insurance claims. Industry representatives argue that undertaking the riskier investments required for community reinvestment places an unnecessary burden on insurers' ability to ensure that claims are paid.

TDI notes that a number of laws and regulations regulate insurers' investments to ensure they have sufficient funds available to pay their claims. Insurers also are subject to Risk Based Capital (RBC) standards, set by the Texas Insurance Commissioner, which requires insurance companies to set aside capital to support the various risks they assume. RBC requirements vary by investment types, with riskier assets subject to higher RBC requirements.

Certified Capital Company (CAPCO) State Economic Development Program

The Comptroller's office and the Texas Treasury Safekeeping Trust Company are responsible for administering the $200 million Texas Certified Capital Company (CAPCO) program. Funded by "Insurance Premium Tax Credits," the CAPCO program supports economic development and generates tax revenues for the state through business growth and job creation. During 2005, the Comptroller's office approved 10 venture capital companies to become CAPCOs.

In Texas, the law requires CAPCOs to invest 30 percent of their capital in "strategically located" businesses and 50 percent in "early stage" businesses within five years of funding. Based on investment commitments from eligible insurance companies (those having premium tax liabilities to the state), each CAPCO requested an allocation of the total $200 million in available premium tax credits.

The tax credits may not be used until 2009 and are restricted to offsetting future insurance premium taxes. Credits may be used starting with the 2008 return at a maximum rate of 25 percent of earned insurance premium tax credits annually.

CAPCOs repay the insurance company investors over time with a combination of earnings on their investments and future tax credits. CAPCOs earn the tax credits by investing in targeted businesses. A CAPCO must meet certain investment criteria and timeframe milestones, pay annual certification renewal fees to the Comptroller's office and adhere to reporting and spending requirements.

CAPCOs may ask the Comptroller's office to determine whether their investments are considered "Qualified Business Investments" under the program rules. The Comptroller's office must review the request and make a determination within a short time frame or the business investment becomes automatically qualified. Through August 31, 2006 the Comptroller had approved 51 of 54 proposed investments representing a total of $57.7 million in potential investments in Texas-based businesses.

The Comptroller's office reviews each CAPCO annually to ensure compliance with program requirements.

Each CAPCO submits reports to the Comptroller's office with a nonrefundable annual fee of $5,000.

By December 15th of each biennium the Comptroller's office is required to report CAPCO-related job creation and program data to the governor, the lieutenant governor, and the speaker of the Texas House of Representatives. The Comptroller's office published the "Certified Capital Companies in Texas Report," on December 15, 2006.

Community Development Corporations (CDCs) in Texas

Financial institutions comply with CRA requirements by making loans to low- and moderate-income borrowers for homes, home-improvement projects and small business ventures. Banks and savings and loans receive favorable credit toward CRA examination ratings by extending loans to and making investments in Community Development Corporations (CDCs).

CDCs provide affordable housing loans for low-income borrowers, manage loan funds for housing development and help residents plan and track new investments. These organizations also find and evaluate home purchase financing and deliver financial literacy, tenant counseling, senior citizen programs and community organizing activities to Texas communities in need.

In 2006, the Texas Association of Community Development Corporations (TACDC) conducted a survey of Community Development Corporations and Community Development Financial Institutions (CDFIs) in Texas assessing affordable housing and loan production information. The survey results are distributed in a biennial publication produced by TACDC, *Building a Future, Contributions of Community Development Corporations in Texas*. This year's publication marks the fifth volume of the survey and builds upon data collected since 1998.

A cumulative total of 259 CDCs and CDFIs responded to the TACDC's Accomplishments Survey in 2000, 2002, 2004 and 2006. Respondents reported producing a total of more than $216 million in loans to community businesses and residents statewide through 2005. Of the 259 survey respondents, 210 reported producing affordable housing or are planning to pursue housing production in 2006-07. Thirty-nine organizations completed or planned to complete commercial or industrial projects, including office space, commercial kitchens and a medical complex, while 25 CDFIs provided housing or business loans through 2005 or planned to do so in 2006-07.

The CDCs indicated in the survey that they built 53,045 affordable housing units through 2005. The housing includes units built in the five principal Texas metropolitan areas—Dallas, Houston, San Antonio, Fort Worth-Arlington and Austin-Round Rock and along the Texas-Mexico border. These CDCs plan to construct an additional 5,089 units between 2006 and 2007. Of the units built between 2004 and 2005, 65 percent were available to those earning between 31 percent and 80 percent of the average median family income (AMFI), and approximately 32 percent are affordable to the lowest income households in Texas earning less than 30 percent AMFI.[56]

Community Reinvestment Issues and Initiatives

Financial Literacy

Millions of young and adult Americans lack knowledge of basic economics and personal financial concepts according to community reinvestment analysts. The 2005-2006 national biennial financial literacy survey by the Jump$tart Coalition for Personal Literacy revealed that the number of 18-24 year olds filing bankruptcy climbed 96 percent in the past 10 years. Noting the rising tide of bankruptcies in the U.S., Lawrence A. Friedman, Executive Director of United States Trustees reported, "Each year, more than one out of every 70 households enters bankruptcy."

Factors contributing to the inability of Americans to make reasonable financial decisions include continued and complex technological enhancements affecting the financial services industry, creative financing programs involving home-related credit transactions and the increased use of credit cards and credit card loans by young people and adults. Fortunately, the Jump$tart Coalition's 2005-2006 survey results showed that U.S. high school seniors modestly increased their basic financial knowledge since 2004. Jump$tart's 2005-2006 financial literacy survey tested 5775 high school seniors from 37 states. The average score was 52.4 percent or one point higher than the 52.3 percent score from the 2003-2004 average.

Only 40.3 percent of U.S. high school seniors understand that they could lose their health insurance if their parents become unemployed. About 22.7 percent of high school seniors realize that interest savings accounts may be taxable if a person's income is high enough, but only 14.2 percent of the students understood that stocks may have higher average returns compared to savings accounts, savings bonds, and checking accounts over the next 18 years even after they were informed that there has never been an 18-year period when this didn't occur.

Students who had never bounced a check had average scores of 53.4 percent, while THOSE who had bounced a check scored 45.8 percent, nearly eight points lower. Students who were unconcerned if a family did not have enough money to pay its bills had average literacy scores of only 43.2 percent. Students who felt that people who retire without much saved for retirement can live pretty well on Social Security alone had lower average scores of 39.9 percent. On the other hand, those who realized it would be tough to live on Social Security scored an average of 56 percent, some of the highest average survey scores.[57]

How does Texas rank in personal financial literacy? Texas ranked first in the list of states with the lowest average credit score of 651 compared with the national average of 578. Texas also spends the least on adult education literacy at just more than $5.00 per capita compared with the national average of $46.65. Reflecting the lack of appreciation of financial literacy, it may be no surprise that Texas ranked 48th in average household net worth among the 50 states. In fact, one in five Texans has zero net worth.[58]

The 79th Legislature passed two financial literacy bills in June 2005 to require financial literacy in Texas schools to help address this problem. House Bill 492, by Rep. Beverly Woolley of Houston, required school districts and open enrollment charter schools to include personal financial literacy instruction starting with the 2006-07 academic year. The schools will use the curriculum created by the National Endowment for Financial Education (NEFE) that meets standards and learning objectives established by the Texas Education Agency (TEA) and State Board of Education.

Senate Bill 851 by Rep Elliot Shapleigh required a financial literacy pilot program to be implemented and tested in 25 school districts before mandating financial education as a requirement for public school graduation.[59]

On January 1, 2007, the TEA submitted its report *Implementation and Effectiveness of the Personal Financial Literacy Pilot Program* to the 80th Texas Legislature as required by House Bill 851 of the last regular legislative session. TEA collaborated with the State Securities Board (SSB) and the OCC on two programs: *Money Smart*, an FDIC program and *Financial Literacy 2010*, a joint project of the Texas SSB, Investor Protection Trust, the North American Securities Administrators Association and the National Association of Securities Dealers.

Twenty-five school districts participated in the pilot projects, and the Dallas Federal Reserve provided teacher training. The Texas State Bar Bankruptcy division provided additional curriculum materials. Some schools implemented the program in the fall of 2006 and others waited until spring of 2007. As of April 2007, TEA had not completed its pilot implementation evaluation results, but TEA reported that an estimated 500 students completed the fall 2006 semester.

Complying with HB 492, TEA amended the Texas Education Code Chapter 74 to require additional personal financial literacy concepts as part of the economics curriculum for public high school graduation. Key concepts to be covered include: understanding the rights and responsibilities of renting a home and home ownership; managing money to make the transition from renting a home to home ownership and starting a small business. The required economics curriculum will teach students how to become a low-risk borrower; methods of prudent stock market investing; using other investment options; beginning a savings program; retirement planning and giving to charitable organizations. Students also will learn about bankruptcy, insurance, the types of consumer bank accounts and related account benefits, how to balance a checkbook and the types of loans available to consumers.[60]

The Federal Reserve Bank of Dallas and the Texas Council on Economic Education planned a series of workshops, "Making Sense of Personal Finance," for Dallas, El Paso, Houston and San Antonio in the summer of 2007. The workshops covered instruction areas mandated in public financial literacy legislation passed by the 80th Texas Legislature including banking and credit, savings and the principles of investing.

The Texas Cooperative Extension, Texas Credit Union Foundation and the National Endowment for Financial Education (NEFE) launched Project NEFE on March 29, 2007. This statewide initiative will bring the free accredited high school financial planning program and training to Texas schools. A team of Project NEFE trainers traveled across Texas to conduct daylong training sessions in Beaumont, Houston, Midland, San Angelo, San Antonio,Waco and other locations. In 2006, the Texas Credit Union Foundation provided almost 40,000 NEFE curriculum copies to community organizations, credit unions and schools across Texas.[61]

Financial Literacy Organizations in Texas

Financial Literacy Coalition of Central Texas has attracted community volunteers from industry, government, private, public and non-profit sectors. Current initiatives include Earned Income Tax Credit education, employee financial education and programs for first-time homebuyers. Spanish-speaking volunteers provide education outreach to Spanish-speaking audiences.

Texas Saves, a partnership launched in January 2005, provides financial literacy training statewide. The organization involves universities, including the Texas A&M Cooperative Extension, financial services companies, community-based organizations, schools and banks. Part of the America Saves national campaign to foster savings and wealth among Americans, Texas Saves' financial education campaign works in partnership with other groups across the country, including the Consumer Federation of America and education enrichment provider Junior Finance Literacy Academy.

Payday, Predatory and Subprime Lending

Payday, predatory and subprime lenders have increased access to credit for many people, but made financial affairs more difficult for many low-income borrowers according to a Ford Foundation Report.[62] Turmoil in the subprime home loan market continues to grow.

Four types of loans—prime, subprime, predatory and payday—dominate the U.S. and Texas lending markets. Traditional "prime" home loans from banks, generally made to borrowers with high credit scores, often have competitive low-interest rates with a minimum of additional charges and loan fees. Subprime, or "B" and "C" rated, loans have higher interest rates and fees than prime loans and are often made to households with relatively negative credit scores and that lack credit histories altogether.[63]

Subprime home loans and subprime mortgage foreclosures affect homeownership, the single most important wealth-generating mechanism families have in the U.S. These mortgages are at least three or four points higher than home loans in the prime market. Almost 60 percent of middle-class family wealth is tied to home equity. For African-American and Hispanic families that share is greater than 88 percent for both groups.[64] A Lehman Brothers investment bank study in 2006 showed that subprime home loans are contributing to the current foreclosure problem. The analysis projected 30 percent losses over time on subprime loans issued in 2006.[65]

Payday loans in the form of small cash advances based on a personal check held for future deposit are provided by stand-alone companies, check cashing outlets, pawn shops, and through online or telephone loan service providers. Payday lending refers to the practice of making short-term loans. Typically, payday loans only require a driver's license and disclosure of income from a job or government benefits.

According to the Office of Consumer Credit Commissioner, practices such as equity stripping, flipping, packing and aggressive marketing are commonly referred to as predatory lending. Equity stripping occurs when a lender targets a prospective borrower with more home equity than debt. The lender offers the borrower a loan against the borrower's home equity that is more than the borrower can repay, resulting in a higher likelihood of foreclosure by the lender.

Texas' home equity constitutional protections limit the amount of home equity a borrower can use to secure a loan at 80 percent, as long as the homeowner retains some equity. Texas laws also restrict borrowers to one home equity loan per year. Texas Finance Code protections for second mortgages ensure lenders evaluate a borrower's ability to repay. Another practice, flipping, happens when a lender repeatedly refinances a borrower's loans within a year and charges high fees and prepayment penalties. Texas' home equity constitutional provisions limit a borrower to one home equity loan per year, and Texas Finance Code prohibits lenders from including prepayment penalties on loan contracts with interest rates of 12 percent or more for loan refinancing. A third predatory lending practice called packing occurs when a lender includes extra fees for unnecessary copy charges, faxes, insurance and making loans to targeted borrowers with minimal verification of the borrower's ability to repay.

Texas home equity laws limit fees to 3 percent of the loan value. Predatory lenders may also tack on unwarranted credit life or disability insurance to mortgage loans, with the cost of credit running as high as $4,000 on a $28,000 loan. Texas Finance Code prohibits lenders from requiring a contracted prepaid insurance premium installment. A fourth predatory lending practice involves aggressive marketing or advertising of consolidation equity loans to pay off auto, credit card and retail debts. In this instance, the borrower may end up with lower monthly payments over a longer period of 15 to 30 years. Predatory lenders make more money from the long-term debt interest of the new loan and ability to foreclose on borrowers' homes for loan default. To address this practice, Texas home equity laws require lender disclosures to borrowers, and Texas Finance Code provisions require lenders to encourage credit counseling to prospective borrowers.[66]

Forces Fueling Subprime Market Foreclosures

Several forces have combined to fuel the growth of the subprime loan market in the U.S. and Texas, and the recent concern over subsequent foreclosures. One force concerns the writing of high-risk "exploding hybrid" mortgages with low interest front-end teaser rates that quickly escalate. A second force involves the application of non-standard mortgage qualification practices to the underwriting of loans. Lenders that fail to escrow property taxes and hazard insurance and brokers that offer incentives to lure unqualified borrowers into unaffordable subprime loans are also strong forces contributing to the rise in subprime market foreclosures.[67]

By far, the most significant force fueling the subprime loan market is the easy availability of high-risk loans with low interest teaser rate payments in the first two years. These "exploding" hybrid mortgages or "2/28s," include a two-year balloon loan that cannot be repaid in monthly installments. The remaining balance must be paid in one lump sum. The "2/28" is an adjustable rate mortgage (ARM) that starts with a two-year teaser "balloon" component with rate adjustments every six months for the rest of the loan term. Generally, the rate of interest climbs 1.5 to 3 percentage points by the end of the second year.[68]

In March 2007, the Center for Responsible Lending estimated that more than 2.2 percent of American families may lose their homes and almost $165 billion in accumulated home wealth. Nationwide, the number of foreclosure filings in 2006 reached 1.2 million, up 42 percent from 2005.[69] As of December 2006, nearly 14 percent of $1.2 trillion in unpaid subprime mortgages were in default. Before the end of 2007, another 1 million loans will be adjusted to higher interest rates and payments. Analysts forecast 800,000 more mortgages may default in 2008.[70]

According to a report by First American Loan Performance, McAllen, Texas, ranked highest among U.S. metro areas with the largest number of subprime mortgage loans (26.8 percent), followed by Memphis, Tenn., (26.0 percent), Sharon, Pennsylvania (24.0 percent) and Miami, Fla. (23.0 percent).[71] According to the Federal Deposit Insurance Corporation, the number of subprime mortgage loans nationally grew to one in every five mortgages in 2006 and 2007. National legislation has been proposed in the House Financial Services Committee to preserve access to credit, aid stable homeownership and stop abuses in the mortgage lending markets. The legislation's critics claim that existing truth-in-lending laws address these issues, and new laws would add burdensome fees and paperwork for creditable borrowers. Also, critics fear that stricter standards could complicate the home-buying process for young buyers.

According to the Mortgage Foundation, Texas recorded nearly 40,000 foreclosure filings in the first quarter of 2007, which is about half of the 80,000 filed in California and 5,000 less than Florida's 45,000 foreclosure filings for the same period. Fortunately, Central Texas experienced subprime loans in fewer than 10 percent of all outstanding mortgages in 2006.[72]

In response to the rising number of foreclosures statewide, in 2007, the 80th Legislature proposed reforms. House Bill 3762 by Rep. Chavez would establish a fiduciary duty for brokers toward borrowers. For refinancing, a new loan would have to show a net benefit for the borrower forcing brokers to disclose the most efficient loan terms available to the buyer. House Bill 2274 by Rep. Rodriguez and companion Senate Bill 987 by Sen. Lucio would make borrowers attend counseling to qualify for high-risk loans of less than $125,000, which have prepayment penalties and variable interest rates. House Bill 1057 by Rep. Parker would require lenders to disclose verbally and in writing the prepayment penalty fees a borrower would have to pay for early loan payoff. House Bill 716 by Rep. Solomons would grant state regulators more powers including the authority to suspend licenses of mortgage brokers after a criminal indictment. Under current law, the state must wait until all criminal proceedings have finished before revoking or suspending a mortgage broker's license.

Agency Strategies to Promote Community Reinvestment in Texas

Each member of the Community Reinvestment Work Group submitted to the Comptroller's office their agencies' strategies to promote community reinvestment in Texas in 2007 and 2008. These strategies do not necessarily reflect the views of all members of the Community Reinvestment Work Group.

Banking Strategies

Most of the financial institutions the Texas Department of Banking (Department) supervises are community banks. Banking regulations require community banks to meet the needs of their communities in order to compete with other financial service providers. Some of these branches are located in low- to moderate-income areas. The Department promotes banks' participation in community reinvestment programs and reviews banks' corrective actions taken on previously cited weaknesses noted in CRA examination reports.

The Department will support financial institutions participating in government-sponsored programs designed to spur community reinvestment. The Department has waived corporate fees for applicants that plan to serve low- and moderate-income areas.

Financial education, or the public's knowledge of financial matters, is an interrelated component of community reinvestment, since consumers who are uneducated about financial matters are ill-prepared to take advantage of community development opportunities and often become the victims of frauds and scams. Unfortunately, due to the lack of basic financial training, many Texans accumulate excessive debt at an early age or remain "unbanked" because of being intimidated or unaware of the benefits of banking services. These individuals, when growing in their own financial education development, improve themselves, their families and their community. The banking system also benefits through enhanced safety and soundness and from customers who are better educated about financial matters and better prepared to take advantage of business opportunities that become available.

To help address this financial education problem, the Department initiated a program to improve Texans' knowledge of financial matters. A financial education coordinator is now employed to serve as the point of contact for information exchange to address financial education issues in Texas. The financial education coordinator collaborates with financial institutions, federal, state and local agencies, minority groups, companies and non-profit organizations to assist Texans in becoming more knowledgeable of financial matters.

The Department's goal is to encourage state-chartered banks in Texas to provide financial education programs in their communities and assist where possible in providing information on available programs and training materials. A number of state-chartered banks have implemented their own financial education programs or are contemplating new programs, but the Department did not possess an inclusive list of these institutions.

In August 2006, the Department requested that all state-chartered banks complete an online survey about their financial education initiatives. Survey responses helped the Department identify those banks that have initiated financial education programs in Texas and those banks that may have other financial programs under development. A total of 154 banks responded to the Department's survey as of September 2006. Results showed that 60 percent of banks in Texas provide customer service in non-English languages and nearly 80 percent of banks in the state do not have a person to coordinate or provide customer financial education. While 60 percent of the state's banks do not conduct financial education training for their communities, almost 90 percent of the survey respondents indicated interest in providing financial education services to people in the communities they serve.[73]

The Department held a number of free banker outreach sessions to be held in Amarillo, Corpus Christi, Dallas, El Paso, Houston, McAllen and San Antonio in April and May of 2007. The goal was to bring together financial education coordinators from different regions of the state, provide financial education training to these coordinators and encourage statewide participation in common educational goals.[74]

Economic Development Strategies

The Small Business Assistance team in the Governor's Division of Economic Development and Tourism Division (EDT) will continue to conduct small business summits in various Texas cities to provide small business owners an opportunity to meet lenders and learn more about securing financing. The team also provides Web-based assistance through the Governor's Office Web site for individuals who are seeking information on starting and financing a business.[75] The Small Business Assistance team will continue to respond to telephone calls and correspondence from Texas citizens who want to learn more about securing financing.

In addition, EDT works with local communities and various state agencies (i.e. Texas Department of Agriculture, Texas Workforce Commission, Texas Commission on Environmental Quality and Texas Department of Transportation) on projects to create jobs and opportunities in Texas communities.

Housing Strategies

The Texas Department of Housing and Community Affairs' (TDHCA) strategies for community reinvestment include disaster relief to areas of east and southeast Texas negatively impacted by Hurricane Rita. The agency also uses increased capital from the TDHCA First Time Homebuyer Program, and through its 2008-09 Legislative Appropriations Request for securing bond fee proceeds to conduct affordable housing market studies and analyses statewide.

In 2006, TDHCA and the Office of Rural Community Affairs allocated $74.5 million in CDBG funds for housing and infrastructure needs in areas affected by Hurricane Rita. In April 2007, the U.S. Department of Housing and Urban Development approved Texas' plan for distributing CDBG funds. Most of the $428 million in federal funds will be directed to rebuilding affordable housing destroyed by Hurricane Rita in 2005.

The City of Houston will receive about $60 million for community and law enforcement expenses incurred for Hurricane Katrina evacuees. The $428 million approved for drawdown by Texas represents less than half of the original $1.2 billion requested for the cost of caring for 400,000 hurricane evacuees.

TDHCA agrees with the research results of recent studies showing that homeownership provides stability for families and communities. TDHCA helped stabilize a number of communities in 2006 with the allocation of $255 million in homebuyer funds. Nearly half of these funds went to Rita "Gulf Opportunity" zones and underserved communities. TDHCA will continue issuing bonds to support the release of more homebuyer funds to provide more stability for communities across Texas.

TDHCA continues to seek funds collected from bond fees from legislation passed in the 78th Legislature, Regular Session. Due to the omission of a budget rider in the state budget bill passed in 2003, TDHCA has been unable to access these funds. Texas Government Code Section 2306.259 directs TDHCA to conduct studies statewide that examine the effect of affordable housing on communities.

TDHCA also continues to allocate approximately $40 million in housing tax credits each year through its Housing Tax Credit program. This public-private partnership helps bring approximately 7,000 new and rehabilitated multifamily units into communities across the state, many of which are located in qualified census tracts.[76] TDHCA supports the use of private capital from tax credits for new and upgraded homes for families in underserved communities.

Insurance Strategies

The Texas Department of Insurance's primary community reinvestment goal is making insurance affordable and available to Texans. TDI's strategies to promote community reinvestment in 2005-06 include encouraging a competitive market by ensuring that consumers can choose from an array of fairly priced products. TDI has adopted new policy forms and endorsements for homeowner's insurance. Endorsements are options, generally to add coverage, in the insurance policy. This gives insurance companies more flexibility in the products they offer.

TDI will continue to study and analyze the effect of credit scoring on insurance availability and affordability in underserved areas. TDI's Consumer Protection Division sponsors educational programs to help consumers determine their available insurance options. The division also provides instructions on how to file a complaint if specific products are not offered in a consumer's area.

Other TDI programs help protect consumers from the loss of insurance even when an insurer becomes insolvent and is placed into receivership. Most insurance policies are covered by one of the state's guaranty funds, which pay claims for insurers that become insolvent. The funds cover up to $100,000 for individual life insurance and annuity policies and up to $300,000 for property and casualty insurance policies.

The 75th Legislature in 1997 required life and health insurance providers, but not property and casualty insurance companies, to report their investments in Texas. Although Texas law does not require separate disclosure of investments in low- and moderate-income communities, some insurers reported their investments voluntarily. The Community Reinvestment Report for 2005 found that insurers held almost $45.6 billion in Texas investments, and insurers identified $764 million of their total investments in economically disadvantaged areas.

Appendix A:
CRA Evaluations

The FRB oversees state-chartered banks that are members of the Federal Reserve System and bank holding companies. The FDIC oversees state-chartered banks and savings banks that are not Federal Reserve members. The OTS regulates the thrift industry, and the OCC regulates national banks, federal branches and agencies of foreign banks, their employees, stockholders and agents. These four banking regulatory agencies regularly examine the financial institutions under their supervision using CRA regulation and examination procedures adopted in 1995.

CRA Examinations and Ratings

Institutions accountable to the FDIC, FRS and OCC follow three asset-size thresholds. First, the "small bank" threshold includes banks that, as of December 31 of either of the prior two calendar years had less than $1.033 billion in assets. Second, the "Intermediate small bank" threshold applies to small banks with assets of at least $258 million and not more than $1.033 billion as of December 31 of both of the two previous calendar years. And third, financial institutions that accept deposits can claim exemption from 2007 CRA data collection requirements of the FRB as a small bank or intermediate small bank if they have less than $1.033 billion as of December 31, 2006 or December 31, 2005.

Institutions regulated by the OTS are "small savings associations" with assets of less than $1 billion as of December 31 of either of the two previous calendar years. Savings associations with assets of less than $1 billion on December 31, 2006 or December 31, 3005 can claim exemption from 2007 CRA data FRB data collection requirements.

The FRB allows small banks, intermediate small banks to submit CRA data to preserve the option of a large bank exam. Small savings associations may provide CRA data to the FRB to preserve their option of a large institution exam.

Large CRA bank examinations include three tests.

1. A lending test accounts for about 50 percent of the CRA bank examination and uses data from the Home Mortgage Disclosure Act and CRA disclosure statements. The lending test evaluates the number and amount of community development loans within the metropolitan statistical area. Investments that qualify for CRA lending test credit include lawful investments, deposits and membership shares or grants with community development as their primary purpose.
2. A service test evaluates the public's accessibility to the bank's financial and community development services. Banks have the option of submitting a strategic plan for the approval by its regulatory agency. Banks that do not extend home mortgages, small business loans, farm loans or consumer loans to retail customers and that have been designated as a wholesale bank by their primary regulator take a limited CRA exam.
3. The investment test examines a bank's record of helping to meet the credit needs of its assessment area through qualified investments that benefit the area(s) or a broader statewide or regional area that includes the bank's assessment area. This test excludes activities already considered under either the lending or service tests. At the bank's option, the OCC will consider a qualified investment made by an affiliate bank when the investment is not already claimed by another financial institution.

The CRA allows a bank to be evaluated under a strategic plan. This option allows the bank to link its CRA objectives to the needs of the community and the bank's own business capacities, goals and expertise. The specific contents of a strategic plan and the OCC's criteria for evaluating these plans are found in 12 CFR 25.27 of OCC's CRA regulation. The criteria include requiring the bank to submit its strategic plan to OCC three months before the proposed plan's effective date; requiring measurable goals for helping meet the credit needs of each assessment area covered by the plan with emphasis on the needs of low- and moderate-income geographies and individuals through lending, investment and services. Among other criteria, the OCC considers the distribution of loans among different geographies, businesses and farms of various sizes, individuals and the extent of community development lending.[77]

Regulatory agencies do not award any particular amount of CRA "credit" for a specific financial or community development service. Large financial institutions may receive CRA ratings of outstanding, satisfactory, low to satisfactory, needs to improve or substantial noncompliance.

Appendix B:
2005-2006 Changes to the Home Mortgage Disclosure Act (HMDA)

The FRB finalized several adjustments and technical amendments in 2005 and 2006 to Regulation C requiring the reporting of public loan data to determine whether financial institutions are serving the housing needs of their communities. Designed to help public officials attract private investment to areas in need and to identify discriminatory lending patterns, Regulation C applies to savings associations, credit unions and mortgage lending institutions.[78]

- Effective January 1, 2003, the FRB required lenders to ask applicants their national origin or race and sex on their loan applications taken by telephone. The telephone application rule now applies to mail and Internet applications.

- Beginning in 2004 for submission by March 1, 2005, amended Regulation C requires lenders to collect and report additional data on home loans and financing for manufactured homes, including loan pricing information, lien status, e.g., secured by a first or subordinate lien, or unsecured.[79]

- As of January 1, 2004, Regulation C began requiring HMDA and CRA reporters to use the new geographic statistical area designations provided by the U.S. Office of Management and Budget (OMB) on June 6, 2003 when collecting data for reporting in March 2005. OMB's revised metropolitan statistical area boundaries led to changes in definitions updated in February 2004 and effective December 2003. Only the terms MSA (used in place of metropolitan area) and MetroDivs (Metropolitan Divisions) will be recognized for HMDA and CRA reporting.

- Also starting January 1, 2004, the FFIEC required lenders to switch to the five-digit number assigned to Metropolitan Statistical Areas, not the previous four-digit number when collecting and reporting HMDA data.[80] For non-depository lenders, effective January 1, 2004, Regulation C began requiring a $25 million volume test[81] to the existing percentage-based coverage test for mortgage bankers that make at least $25 million in mortgages annually. For 2004 data collection, the asset threshold for depository lenders was raised to $33 million from $32 million and remained unchanged at $10 million or less for non-depository institutions. The FFIEC uses the loan data submitted under the HMDA to create reports for each metropolitan area in the U.S. In 2004, about 8,121 financial institutions provided a total of 42 million loan records for calendar year 2003.

- The FRB raised the asset exemption threshold for depository institutions to $35 million in December 2005 for 2006 data collection, but left the threshold unchanged for nondepository institutions.

- Next, the FRB raised the asset exemption to $36 million in December 2006 for 2007 data collection. The FRB left the threshold for nondepository institutions for 2007 data collection unchanged at $10 million or less when combined with a parent corporation's assets or originated 100 or more home purchase loans including refinancings. Nondepository institutions may combine their assets of parent corporations in the preceding calendar year.[82]

Appendix C:
Texas Legislation

Legislation Passed by the 79th Legislature in 2005

A number of Texas legislative changes occurred since the 2005 update. To assist Texas homebuyers, the 2005 Legislature passed:

- **House Bill 467**, which expands the Economically Distressed Areas Program (EDAP) to supply water and sewer to low income communities of the state. The bill will make no-interest loans and grants available from the state for impoverished areas without water and sewer services.
- **House Bill 525** to help prevent the displacement of working and retired, lower income individuals and families from East Austin. The bill creates opportunities for low- and moderate-income families to own homes and authorizes the city to create a development district known as the Homestead Preservation District through land trusts, land banks and tax increment financing dedicated to city-certified community housing development organizations.
- **House Bill 1099**, which transferred farm worker housing inspection authority to the Texas Department of Housing and Community Affairs (TDHCA) from the Texas Department of Health (TDH).
- **House Bill 1582**, which directed TDHCA and the Texas Savings and Loan Department to create a commission of experts to report to the Texas Legislature by September 1, 2006 on mortgage foreclosure rates in Bexar, Cameron, Dallas, El Paso, Harris and Travis counties. Dr. Elizabeth Mueller of the Texas Low Income Housing Information System board led the research and presented the study's findings. The study reported on the relationship of mortgage terms to the foreclosure rate, socioeconomic and geographic influences on foreclosures, secondary market securitization of mortgages and consumer education efforts to prevent foreclosures. The study also recommended how to reduce foreclosures across Texas. A summary of the commission's results are found in Appendix D.
- **House Bill 1823** established new protections for contract-for-deed and rent-to-own buyers. The bill gives buyers a legal right to convert contracts-for-deed into traditional mortgages and ends the abuses of excessive late fees and immediate termination of the "option to buy" in rent-to-own programs
- **House Bill 2491** amendments were passed to make the elderly homestead exemption occur automatically at age 65.
- **Senate Bill 356**, which created a "land bank" program for Houston, Texas to, allow Houston to sell tax-foreclosed and delinquent property to organizations for affordable housing development. There is no available funding for the program. The land banking aspect of the bill ends requirements for properties to be auctioned in public to collect back taxes. The bill allows properties to be sold below market price by the City of Houston and sold to organizations that will build affordable housing.
- **Senate Bill 833** requires the city of Austin, Texas, to set aside 25 percent of tax increment financing zones' (TIFs) money to fund low-income housing until 10 percent of a neighborhood's total housing stock is affordable for families that earn below $35,550 per year. The legislation requires affordable housing units to be included in planned developments along the new Capital Metro light rail system.
- **Senate Bill 1186** makes it easier for active U.S. service members and domestic violence victims to terminate their apartment leases.

Appendix D:
Highlights of "A Study of Residential Foreclosures in Texas"

House Bill 1582, passed by the 79th Legislature, required a study of mortgage foreclosure activity in Bexar, Cameron, Dallas, El Paso, Harris and Travis counties. The Texas Department of Housing and Community Affairs (TDHCA) coordinated the study that evaluated:

1. the extent to which the terms of mortgages are related to the foreclosure rate and whether such terms could be offered in a manner to reduce the likelihood of foreclosures;
2. the socioeconomic and geographic elements characterizing foreclosures;
3. the securitization of mortgages in the secondary market and its effect on foreclosures;
4. consumer education efforts to prevent foreclosures; and
5. recommendations to reduce foreclosures and the foreclosure rate across the state.

HB 1582 established an advisory committee (Committee) to direct the study. This committee included one representative from the Texas Housing Research Consortium at the University of Texas at Austin who also served as Chair, TDHCA's executive director; Texas Savings and Mortgage Lending (SML) Commissioner, four members assigned by TDHCA who represent community and consumer interest and four members appointed by SML that represent the mortgage lending industry.

Texas leads the nation in terms of the total number of foreclosures. Comparing foreclosure statistics by state from July 2005 to June 2006, Texas had 36,362 foreclosures. The committee also studied foreclosure rates for six counties in Texas: Bexar, Cameron, Dallas, El Paso, Harris and Travis. Harris County (6,119 foreclosures) ranked highest in the number of total foreclosures for the period June 2005 through May 2006. Dallas County had 6,107 foreclosures during this period, followed by Bexar (2,440), Travis (1,195), El Paso (476) and Cameron (354). The data comes from the Foreclosure.com Web site's reported number of real estate owned (REO) properties which were purchased by the mortgage holder following a foreclosure sale.[83]

According to the study, the number of pre-foreclosures and actual foreclosures varies among the states due to differences in individual state foreclosure process requirements and housing market conditions. The pre-foreclosure period can include the initial public default notice until the time that the property is sold at auction. Between states, the notification requirements and length of different foreclosure proceeding stages also vary.

Generally, Texas has lower residential property appreciation rates compared to California, Florida and Nevada where the number of foreclosed properties sold is below the number of posted foreclosures. According to the study, homeowners in California, Florida and Nevada have less difficulty selling properties in foreclosure to cure default and profit. Texans, however, have more difficulty selling property at a high enough price to successfully cure a mortgage default.

A borrower's ability to make mortgage payments or default on loans is usually the primary cause of delinquency. The study reported four primary factors contributing to the inability to meet monthly mortgage payments. The first factor involves changes in personal situation, including job loss or reduction in income and major uninsured medical crises. The second factor relates to the failure to comprehend or plan for mortgage obligations. A third factor includes being a victim of unlawful lending or unscrupulous mortgage practices including flipping, loan churning, excessive fees, lending without consideration of a borrower's ability to pay, fraud and abuse. The fourth factor involves a borrower who voluntarily participates in fraudulent activities to qualify for a loan or profit from a dishonest transaction.

Comparing estimated foreclosure timelines by state, the study committee found that Texas' foreclosure process is quick, short and simple compared to comparably sized states like California and Florida. Texas is a "power of sale" state that does not require a judicial foreclosure process. Foreclosures can occur without court involvement. States with a comparable foreclosure rate, but longer foreclosure periods include Colorado (166 days), Indiana (251 days), Michigan (90-425 days), Ohio (217 days) and Utah (138 days). Texas' non-judicial foreclosure process from delinquency to foreclosure sale can be as short as 41 days.[84]

The study described current foreclosure reduction strategies and laws in Texas, reviewed legislated procedures across the U.S., and summarized their effectiveness. The study group recommended areas needing further research and improvements to current foreclosure prevention efforts. Two common trends were identified in the study:

- the correlation between high foreclosure rates and particular demographic data was found across five of the six counties evaluated. El Paso County's high concentrations of minority populations did not correlate to higher foreclosure rates, and
- residential foreclosure rates are tied to lower income levels and increased use of higher rate loans.

The study recommended further analysis of Texas-specific data on the causes of foreclosure, including factors that result in defaults on loans. Analysis could be provided through funded academic research or the mandated data collection requirements. The study Committee suggested that the Legislature appropriate funds to:

- fund enforcement of stronger fraud laws;
- broaden multilingual education and outreach efforts to increase borrower awareness and options to settle delinquencies; and
- provide financial support to expand buyer education programs and organizations to help buyers with the foreclosure process in Texas.

The study committee recommended that the Legislature:

- adequately fund enforcement of stronger fraud laws in Texas;
- expand multilingual education efforts for borrowers to work loan delinquencies; and
- provide support for expanding homebuyer education initiatives and of organizations to counsel borrowers in the foreclosure process.

Acknowledgements

Comptroller of Public Accounts

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Byron Beasley

Office of the Governor

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Texas Comptroller of Public Accounts
Publication# 96-643 – Updated October 2007

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